College Accounting

FIFTH EDITION

By

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PREFACE

This textbook was prepared for students of accounting, secretarial science, and business administration. The aim of the book is to provide such students with an understanding of the principles and practice of modern business accounting. Training in accounting is advantageous to those who aspire to desirable positions in business and industry, in many of the professions, and in numerous branches of government.

Accounting is an indispensable tool of business management. Besides the managers, present and potential owners and creditors of businesses use accounting reports as a basis for judgments, decisions, and action. Adequate, complete, and detailed business records are needed in order to comply with various governmental statutes and regulations, particularly federal and state income tax laws, labor laws, and the requirements of the social security program.

The principles of accounting and financial reporting have wide application. The differences between the records kept for a small business or professional practice and the accounting system of a giant corporation are largely differences of scope and degree. Accounting procedures are adaptable to a wide variety of situations and requirements. This textbook presents the basic principles of modern record keeping and accounting theory, and explains and illustrates the adaptation of these fundamentals to various business and professional situations.

Numerous forms are illustrated in this textbook. Official forms were used as a basis for the illustrations of governmental forms. The accounting forms illustrated contain standard rulings and headings. Thus, accounting forms similar to those shown in the illustrations are available for actual business use. Such forms may be obtained at all leading stationery stores or from dealers in accounting forms.

Workbooks and practice sets are available for use with this book. The text is divided into a number of study assignments. The workbooks provide correlated exercises and practical accounting problems for each assignment. Additional problems are provided for such remedial work as may be necessary. The practice sets furnish realistic cases of accounting for different types of undertakings including retail and wholesale mercantile establishments, personal service enterprises, and an industrial concern.

The authors acknowledge their indebtedness and express their appreciation to the business executives, accountants, experienced instructors, and other professional people whose advice and suggestions contributed to the preparation of this textbook.

J. F. S.
C. B.
A. B. C.

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Unit One

ELEMENTS OF ACCOUNTING

I ASSETS, LIABILITIES, AND PROPRIETORSHIP

Record Keeping. The need for record keeping is universal. Individuals, families, social organizations, civic enterprises, governmental units, and business organizations should keep records of their financial affairs and operations. Tax laws, social security laws, unemployment compensation laws, workmen's compensation laws, wage and hour laws, and other laws require those who are subject to such laws to keep certain records. For example, under the federal income tax regulations each taxpayer is required by law to maintain such accounting records as will enable him to make a return of his true income. Penalties may be imposed for failure to keep the required records. From appropriate records, a business organization is able to ascertain its financial position at any time and the results of its operations over any given period of time.

When records of any desired information are kept, the process may properly be termed *record keeping.* The data recorded may be of historical, statistical, or financial nature. The keeping of a diary in which certain events, financial and otherwise, are recorded in chronological order is record keeping; however, such record keeping does not necessarily require a knowledge of accounting principles. On the other hand, if a complete record of all financial affairs and operations is maintained in an approved manner that is subject to proof of accuracy, a knowledge of accounting principles is required.

Double-Entry Bookkeeping. The need for a method of record keeping that facilitates proof of accuracy led to the origin of a system of *double-entry bookkeeping.* The fundamental principle of double-entry bookkeeping is the principle of balance. It is this principle that differentiates double-entry bookkeeping from other types of record keeping. In double-entry bookkeeping at least two entries are made in recording each transaction. This provides a means of proof. If each transaction is recorded so that one entry may be checked or balanced against another entry for the purpose of proof, then the aggregate of all entries may be proved periodically by means of a trial balance.

A knowledge of double-entry bookkeeping is of value to everyone engaged in business whether as an employer or as an employee, regardless of whether his income is derived from the conduct of a business enterprise, from professional fees, or from wages received as compensation for personal services. It is also of value to self-employed individuals who have no employees but who are engaged in some business or professional enterprise. A knowledge of double-entry bookkeeping may prove of great value even though it is not used vocationally. While bookkeeping experience may prove of great promotional value as a steppingstone, a sound knowledge of the principles of double-entry bookkeeping may prove of even greater value in the successful administration of a business or of any department of a business enterprise.

Accounting. There is no clear-cut distinction between bookkeeping and accounting; however, bookkeeping is often referred to as the recording branch of accounting. Accounting also involves the summarization and the analysis of the activities of a business enterprise. The person who keeps books of account may be referred to as a bookkeeper. The person who analyzes and interprets accounts as an aid to sound business management may be referred to as an accountant. One person may perform both functions. Some bookkeeping experience is considered essential to success as an accountant. An accountant who offers his services to the public on a fee basis is known as a public accountant. If, after passing an examination, he is certified by the state, he is known as a *certified public accountant* (C.P.A.).

Accounting Elements. If complete records are to be maintained, all transactions and operations that affect the accounting elements should be recorded. The accounting elements consist of *assets, liabilities,* and *proprietorship.*

(a) What is owned constitutes assets.
(b) What is owed constitutes liabilities.
(c) Any excess of assets over liabilities constitutes proprietorship.

Assets. Property owned, such as money, notes, accounts receivable, merchandise, bonds, furniture, fixtures, automobiles, buildings, land, and anything that is of value to the owner or that is available for the payment of debts constitute assets. Although it is possible to engage in a business activity without ownership of property, usually some property is owned. For example, a dentist must of necessity have some instruments with which to work. Office equipment, laboratory equipment, and dental supplies may be owned. He may have some money in a bank. Such property, together with other property that he may have purchased as an investment, constitutes his assets.

A merchant must have merchandise to sell; he must have money to pay his debts; he may have store equipment; customers may owe him for merchandise sold on credit. Amounts due from customers from the sale of merchandise on credit are known as *accounts receivable.* Thus merchandise, money, store equipment, and accounts receivable may constitute his assets.

Liabilities. Debts owed or financial obligations to creditors constitute liabilities. Ordinary debts arising from purchases on credit are known as *accounts payable;* debts evidenced by notes are known as *notes payable.* If the dentist referred to previously had purchased instruments, dental supplies, office equipment, or other property on credit, he would have incurred liabilities in the form of either accounts payable or notes payable. If he made purchases on credit, the obligations incurred would be known as accounts payable; if he gave notes in connection with such purchases, the obligations incurred would be known as notes payable.

Proprietorship. The term *proprietorship* represents the net worth or capital of an individual or an enterprise. If there are no liabilities, the total value of the property owned will represent the *net worth* or *capital* of the owner. When liabilities exist, the sum of the liabilities must be deducted from the total value of the assets owned in order to find the net worth or capital of the owner.

It is possible for a person without capital of his own to engage in a business enterprise by borrowing money or purchasing on credit the property needed to operate the enterprise. In such case, his liabilities will be equal to his assets until he succeeds in increasing the assets without a corresponding increase in the liabilities, or until he succeeds in decreasing his liabilities without a corresponding decrease in his assets. Ordinarily a person who engages in any business enterprise or in the conduct of a profession makes some investment in the property that he acquires for use in conducting his affairs. If he is successful in operating at a profit, his proprietorship may be increased. The amount of his proprietorship may be determined at any time by ascertaining the difference between the total value of the property owned (assets) and the amount of the debts owed (liabilities).

The Accounting Equation. As previously explained, there are three elements that must be accounted for under the double-entry system of bookkeeping — assets, liabilities, and proprietorship. It is fundamental to the double-entry system that the total amount of the assets is always equal to the sum of the liabilities and the proprietorship. Thus the following may be said to be the fundamental accounting equation:

$$\text{Assets} = \text{Liabilities} + \text{Proprietorship}$$

When the amounts of any two elements of the equation are known, the amount of the third element can always be calculated.

W. C. Taylor is an architect. On December 31 his records show that he owns property valued at $12,400. He owes creditors $400 for merchandise purchased on credit and owes the bank $500 on a note.

Mr. Taylor's assets amount to $12,400 and his liabilities amount to $900. The amount of his proprietorship may be calculated by subtraction ($12,400 − $900 = $11,500). These facts may be expressed in equation form as follows:

$$\text{Assets } \$12{,}400 = \text{Liabilities } \$900 + \text{Proprietorship } \$11{,}500$$

If Mr. Taylor's assets are known to amount to $12,400 and his proprietorship is known to amount to $11,500, the amount of his liabilities can be calculated by subtraction ($12,400 − $11,500 = $900). If his liabilities are known to amount to $900 and his proprietorship is known to amount to $11,500, the amount of his assets can be calculated by addition ($900 + $11,500 = $12,400).

If Mr. Taylor desires to increase his proprietorship, he must either (a) increase the value of his assets without a corresponding increase in the amount of his liabilities or (b) decrease the amount of his liabilities without a corresponding decrease in the value of his assets. Such results may be obtained by operating at a *profit* or by investing additional assets. In other words, to increase his proprietorship without investing additional assets, he must conduct his affairs in such a manner that his income will exceed his expenses.

If Mr. Taylor, during the following year, succeeded in increasing the total value of his property to $15,000 without a corresponding increase in the amount of his liabilities, his proprietorship would be increased to $14,100, an increase of $2,600. These facts may be expressed in equation form as follows:

$$\text{Assets } \$15{,}000 = \text{Liabilities } \$900 + \text{Proprietorship } \$14{,}100$$

On the other hand, if Mr. Taylor increased the total value of his property to $15,000 and at the same time increased the amount of his liabilities to $3,500, there would be no increase in his proprietorship, as shown by the following equation:

ASSETS $15,000 = LIABILITIES $3,500 + PROPRIETORSHIP $11,500

If Mr. Taylor paid all of his obligations so that he had no liabilities at the end of the year and his property remained the same in amount as at the beginning of the year, his proprietorship would be increased to $12,400, an increase of $900. These facts may be expressed in equation form as follows:

ASSETS $12,400 = LIABILITIES 0 + PROPRIETORSHIP $12,400

When there are no liabilities, the proprietor's net worth will always be equal to his total assets.

Transactions. The activities of an enterprise are usually referred to as *transactions.* Producing, buying, selling, transporting, and servicing are common transactions. A transaction is an exchange of values. The values are expressed in terms of money. The following typical transactions are analyzed to show that each transaction represents an exchange of values:

TYPICAL TRANSACTIONS	ANALYSIS OF TRANSACTIONS
(a) Purchased equipment for cash, $250.	Money is exchanged for equipment.
(b) Received cash in payment of professional fees, $125.	Professional service is rendered in exchange for money.
(c) Paid office rent, $100.	Money is exchanged for the right to use property.
(d) Received cash in payment of interest on a savings account, $75.	Money is received in exchange for the use of money.
(e) Paid a debt owed to a creditor, $300.	Money is given in settlement of a debt that may have resulted from the purchase of property on credit or from services rendered by a creditor.
(f) Paid wages in cash, $90.	Money is exchanged for services rendered.
(g) Purchased merchandise for cash, $400.	Money is paid in exchange for merchandise.
(h) Purchased merchandise on credit, $200.	A debt known as an account payable is incurred in exchange for merchandise.
(i) Sold merchandise for cash, $140.	Money is received in exchange for merchandise.
(j) Sold merchandise on credit, $85.	Merchandise is exchanged for credit known as an account receivable.

Effect of Transactions on the Accounting Equation. Each transaction affects one or more of the three elements of the accounting equation. For example, the purchase of a truck for cash represents both an increase and a decrease in assets. The assets are increased because a truck is acquired;

the assets are decreased because cash is disbursed. If the truck were purchased on credit, thereby incurring a liability, the transaction would have resulted in an increase in assets (truck) with a corresponding increase in liabilities (accounts payable). Neither of these transactions has any effect upon the proprietorship element of the equation.

The effect of any transaction on the accounting elements may be indicated by addition and subtraction. Assume that on January 1 the status of an enterprise is indicated by the following equation:

ASSETS $19,400 = LIABILITIES $1,900 + PROPRIETORSHIP $17,500

The effect of the following transactions completed during January is shown at the right:

	A $19,400	= L $1,900	+ P $17,500
(a) Purchased a truck for $3,000 cash.			
An asset (truck) is increased $3,000:	+ 3,000		
An asset (cash) is decreased $3,000:	− 3,000		
(b) Purchased office equipment on credit, $1,800.			
An asset (office equipment) is increased $1,800:	+ 1,800		
A liability (account payable) is increased $1,800:		+ 1,800	
(c) Paid $900 to apply on office equipment previously purchased on credit.			
An asset (cash) is decreased $900:	− 900		
A liability (account payable) is decreased $900:		− 900	
(d) Proprietor withdrew $200 in cash for personal use.			
An asset (cash) is decreased $200:	− 200		
Proprietorship is decreased $200:			− 200
	A $20,100	= L $2,800	+ P $17,300

After giving effect to the foregoing transactions the status of the enterprise on January 31 was indicated by the following equation:

ASSETS $20,100 = LIABILITIES $2,800 + PROPRIETORSHIP $17,300

Thus while each transaction affected one or more elements of the equation, the equality of the elements was not disturbed. Changes that take place in the value of the accounting elements never affect the equality of the elements. It is a basic principle of double-entry bookkeeping that the total value of the assets at all times is equal to the sum of the liabilities and the proprietorship.

PRACTICE ASSIGNMENT No. 1. A workbook is provided for use with this textbook. Each practice assignment in the workbook is referred to as a report. The work involved in completing Report No. 1 requires a knowledge of the principles developed in the preceding study assignment. Before proceeding with the following study assignment, complete Report No. 1 in accordance with the instructions given in the workbook.

II THE THEORY OF DEBIT AND CREDIT

The Account. A business or professional enterprise may have various types of assets and liabilities. In order to provide the information needed in the operation of an enterprise it is necessary to keep a separate record of each type of asset, each type of liability, and the proprietorship element in a manner that will show the changes resulting from the operations of the enterprise. A device for grouping and summarizing the changes caused by transactions is known as an *account*. The titles and the number of accounts required in recording the operations of a business vary widely depending upon many factors, such as the nature of the business, the volume of business, the type of business organization, and the information desired by the management.

The "T" Account. While there are many forms of accounts in general use, the simplest form of account is the "T" account. This form of account is widely used by instructors as a teaching aid and by accountants for memorandum purposes. It consists of a form ruled in the shape of the letter "T." This form of account is used frequently in this book to illustrate the principles discussed.

Each account should be given a title indicative of the nature of the information recorded therein. For example, an account of money received and disbursed is usually entitled Cash. The title of an account should be written on the horizontal line at the top of the form. The space at the left of the perpendicular line is known as the *debit side* of the account; the space at the right of the perpendicular line is known as the *credit side* of the account. Amounts entered on the left side of the account represent debit entries; amounts entered on the right side of the account represent credit entries. The difference between the sum of the debit entries and the sum of the credit entries represents the *balance* of the account.

TITLE

Debit side	Credit side

Debits and Credits. The terms *debit* and *credit* are used to describe the effect of transactions on accounts. The only effect a transaction may have on any account is either to increase or to decrease its amount or balance. By arranging the account with two sides or columns for recording increases and decreases, the effect of each transaction may be indicated by the position of the entries in the account.

In the case of an asset account, a debit entry indicates an increase in the amount or value of the asset, while a credit entry indicates a decrease in the amount or value of the asset. When all increases are recorded on the left or debit side and all decreases are recorded on the right or credit side of the account, it is possible to ascertain the present amount or value at any time by adding both sides and subtracting to find the difference or balance of the account. Asset accounts always have debit balances as long as any value remains. Thus a cash account will always have a *debit balance* as long as there is any cash available or on hand.

ASSETS

Debit to record increases	Credit to record decreases

In the case of a liability account, a debit entry indicates a decrease in the amount of the liability, while a credit entry indicates an increase in the amount of the liability. When all decreases are recorded on the left or debit side and all increases are recorded on the right or credit side of the account, it is possible to ascertain the amount owed at any time by adding both sides and subtracting to find the difference or balance of the account. Liability accounts always have credit balances as long as there is any amount owed. Thus an account with accounts payable will always have a *credit balance* as long as there is any amount owed to creditors.

LIABILITIES

Debit to record decreases	Credit to record increases

In the case of the proprietor's capital account, a debit entry indicates a withdrawal of assets such as cash or merchandise by the proprietor for personal use or a decrease in proprietorship resulting from the operations of the business at a loss; a credit entry indicates an increase in the amount of the proprietor's investment in the enterprise or an increase in proprietorship resulting from the operations of the enterprise at a profit. When all decreases are recorded on the left or debit side and all increases are recorded on the right or credit side of the account, it is possible to ascertain the proprietor's net worth or present capital at any time by adding both sides and subtracting to find the difference or balance of the

PROPRIETOR

Debit to record decreases	Credit to record increases

account. As long as the sum of the assets exceeds the sum of the liabilities, the proprietor's capital account will have a credit balance; when the sum of the liabilities exceeds the sum of the assets, the proprietor's capital account will have a debit balance.

Debits are always recorded on the left side and credits on the right side of an account regardless of whether it is an asset, liability, or proprietorship account. In the case of asset accounts, debit entries represent increases, while credit entries represent decreases. The opposite is true in the case of liability and proprietorship accounts, that is, debit entries represent decreases, while credit entries represent increases.

Transactions Affecting Asset Accounts. If a transaction results in an increase in an asset, it should be recorded in such a manner that the amount of the increase may be added to the account affected. An increase in an asset should, therefore, be recorded as a debit to the proper asset account. If a transaction results in a decrease in an asset, it should be recorded in such a manner that the amount may be subtracted from the account affected. A decrease in an asset should, therefore, be recorded as a credit to the proper asset account.

To illustrate the principles being discussed here, a few selected transactions will be analyzed and recorded in "T" accounts. The transactions are not related and the dates are purposely omitted.

(a) Paid $100 for office equipment.

Since this transaction represents an exchange of one asset for another asset, it should be recorded in such a manner as to show that an increase in one asset is offset by a decrease in another asset. It is advisable, therefore, to keep separate asset accounts for office equipment and cash. Office Equipment should be debited for $100 to record the increase in assets, while Cash should be credited for $100 to record the decrease in assets. The effect of the transaction is illustrated by the debit and credit entries in the following "T" accounts:

OFFICE EQUIPMENT

(a)	100.00		

CASH

		(a)	100.00

Transactions Affecting Liability Accounts. If a transaction results in an increase in a liability, it should be recorded in such a manner that the amount of the increase may be added to the account affected. An increase in a liability should, therefore, be recorded as a credit to the proper liability account. If a transaction results in a decrease in a liability, it should be recorded in such a manner that the amount may be subtracted from the account affected. A decrease in a liability should, therefore, be recorded as a debit to the proper liability account.

(b) Purchased office equipment on credit for $125.

Bills

Since a debt known as an account payable is incurred in exchange for office equipment, this transaction should be recorded in such a manner as to show that an increase in assets is offset by an increase in liabilities. It is advisable, therefore, to keep separate accounts for office equipment and accounts payable. Office Equipment should be debited for $125 to record the increase in assets, while Accounts Payable should be credited for $125 to record the increase in liabilities. The effect of the transaction is illustrated by the debit and credit entries in the following "T" accounts:

Office Equipment			
(b)	125.00		

Accounts Payable			
		(b)	125.00

Transactions Affecting the Proprietor's Account. If a transaction results in an increase in proprietorship, it should be recorded in such a manner that the amount of the increase may be added to the account affected. An increase in proprietorship should, therefore, be recorded as a credit to the proprietor's account. If a transaction results in a decrease in proprietorship, it should be recorded in such a manner that the amount may be subtracted from the account affected. A decrease in proprietorship should, therefore, be recorded as a debit to the proprietor's account.

(c) Matthew Morgan invested $1,000 in a radio and television service enterprise.

Since this transaction represents the receipt of cash as a proprietary investment, it should be recorded in such a manner as to show that the amount of the assets acquired by the enterprise is offset by the proprietor's capital. It is advisable, therefore, to keep a separate asset account for cash and a proprietorship account for Matthew Morgan. Cash should be debited for $1,000 to record the asset acquired, while Matthew Morgan, Proprietor should be credited for $1,000 to record the amount of his investment in the enterprise. The effect of the transaction is illustrated by the debit and credit entries in the following "T" accounts:

CASH		MATTHEW MORGAN, PROPRIETOR	
(c) 1,000.00			(c) 1,000.00

Types of Proprietorship Accounts. There are two types of proprietorship accounts as follows:

(a) Permanent proprietorship accounts.

(b) Temporary proprietorship accounts.

When an individual engages in a business enterprise on his own account, it is known as a *sole proprietorship.* In such case the account in which the proprietor's investment is recorded is known as his permanent proprietorship or capital account. When two or more individuals engage in a business enterprise as partners, it is customary to keep a separate account for each partner in which his investment is recorded.

Under the *private enterprise system* the proprietors expect to increase their proprietorship through profitable operations. There are two types of transactions that affect proprietorship. First, there are some transactions that produce income or result in a profit or gain, thereby causing the proprietorship to be increased. Second, there are some transactions that represent an expense or result in a loss, thereby causing the proprietorship to be decreased. Temporary proprietorship accounts are used to record such increases and decreases to provide detailed information regarding the operations of the business.

Transactions Affecting Income Accounts. Accounts representing increases in proprietorship may be used to record income, gains, or profits. The particular accounts to be kept in recording the increases depend upon the nature or the source of the income. A wage earner may derive most of his income from salary or wages, but he may also derive some income from investments. He should keep separate income accounts so that he may know the total amount of his income from each source.

A professional man, such as a doctor, a lawyer, a dentist, or a public accountant, may derive his principal income from fees, but he may have other income such as interest on notes and bonds, dividends on stocks, or rent from an apartment building that he owns as an investment. He should keep separate income accounts so that at the end of each year he may know the total amount of his income from each source.

The proprietor of a business enterprise may derive his income from fees received for services rendered or from the sale of merchandise or manufactured goods. He may receive income from other sources. He, also, should keep separate accounts so that at the end of each year he may know the total amount of his income from each source. All of these persons will need such information in preparing their income tax returns for each year.

(d) Matthew Morgan received $40 for services rendered in installing a television set.

Since this transaction involves the receipt of income in cash, it should be recorded in such a manner as to show that an increase in assets is offset by an increase in income. It is advisable, therefore, to keep an asset account for cash and another account for income from services. The latter account is a temporary proprietorship account. Cash should be debited for $40 to record the increase in assets, while Income from Services should be credited for $40 to record the increase in income. The effect of the transaction is illustrated by the debit and credit entries in the following "T" accounts:

CASH

(d)	40.00		

INCOME FROM SERVICES

		(d)	40.00

Transactions Affecting Expense Accounts. Accounts representing decreases in proprietorship may be used to record costs, expenses, or losses. The particular accounts to be kept in recording the decreases in proprietorship depend upon the type or the nature of the expenses and the losses incurred. Separate accounts should be maintained to record the different types of expenses and losses so that at the end of each year the proprietor may have the detailed information needed in preparing his income tax return for the year and in planning his future operations.

(e) Matthew Morgan paid $75 for a month's rent on his shop.

Since this transaction involves the payment of rent in cash, it should be recorded in such a manner as to show that an increase in expenses is offset by a decrease in assets. It is advisable, therefore, to keep an expense account for rent and an asset account for cash. The rent expense account is a temporary proprietorship account. Rent Expense should be debited for $75 to record the increase in expenses, while Cash should be credited for $75 to record the decrease in assets. The effect of the transaction is illustrated by the debit and credit entries in the following "T" accounts:

RENT EXPENSE

(e)	75.00		

CASH

		(e)	75.00

The Accounting Period. When the *accounting period* is a year ending on December 31, it is known as a *calendar year*. When the accounting period is a year ending on the last day of any month other than December, it is known as a *fiscal year*. When the accounting period is less than a year, it is known as a *fiscal period* and may represent a period of one month, three months, six months, or any other part of a year.

At the end of each accounting period the temporary proprietorship accounts representing increases and decreases in proprietorship should be summarized so that the net increase or the net decrease in proprietorship for the period may be ascertained. The method of summarizing the increases or the decreases in proprietorship at the end of each accounting period will be explained later. It is sufficient to understand at this point that the function of the temporary proprietorship accounts is to provide a record of the increases and the decreases in proprietorship during an accounting period.

Application of Principles. J. D. Knight is the proprietor of an advertising agency. In keeping his accounts, he follows the practice of recording income on the basis of cash receipts and recording expenses on the basis of cash disbursements; that is, income is not recorded until received in cash and expenses are not recorded until paid in cash. At the beginning of the accounting period, he owned the following assets:

Cash, deposited in a checking account at the Second National Bank, $900.

Office equipment, consisting of desks, chairs, typewriters, a mimeograph, a multigraph, and other miscellaneous equipment, $5,000.

An automobile, used exclusively for business purposes, $2,100.

Since Mr. Knight had no debts or obligations, his financial condition may be expressed in equation form as follows:

ASSETS $8,000 = PROPRIETORSHIP $8,000

In opening accounts for the assets, each asset account was debited for the value of the property represented; hence Cash was debited for $900, Office Equipment for $5,000, and Automobile for $2,100. In opening a proprietorship account for Mr. Knight, the account was credited for $8,000. The accounts are reproduced on page 23.

Before recording a transaction, the effect of the transaction upon the accounts involved must be determined by analysis. A series of selected transactions will be analyzed and entered in appropriate "T" accounts to illustrate the procedure.

NARRATIVE OF TRANSACTIONS

(a) Paid one month's rent in advance, $100.

Analysis: The payment of rent involves an increase in expense and a decrease in cash. This transaction should be recorded by debiting Rent Expense and by crediting Cash for $100.

(b) Purchased office equipment from Whitcomb and Riley on credit, $300.

Analysis: This transaction resulted in an increase in assets and created a liability. It should be recorded by debiting Office Equipment and by crediting Accounts Payable for $300. Accounts Payable is a summary account in which are recorded all transactions representing increases or decreases in the amounts owed to creditors.

(c) Received $410 from J. T. Thompson and Co. in full payment for services rendered.

Analysis: This transaction involves an increase in cash and an increase in income. It should be recorded by debiting Cash and by crediting Income from Advertising Fees for $410,

(d) Paid gas and electric bill, $8.75.

Analysis: This transaction involves an increase in expense and a decrease in cash. It should be recorded by debiting an expense account entitled Gas and Electricity and by crediting Cash for $8.75.

(e) Gave the Community Chest $25 as a charitable contribution.

Analysis: This transaction involves an increase in expense and a decrease in cash. It should be recorded by debiting Charitable Contributions and by crediting Cash for $25.

(f) Purchased government bonds for $187.50.

Analysis: This transaction involves an exchange of assets. The purchaser acquires the asset government bonds and decreases the asset cash. The transaction should be recorded by debiting Government Bonds and by crediting Cash for $187.50.

ACCOUNTS OF J. D. KNIGHT

Cash

	900.00	(a)	100 00
(c)	410.00	(d)	8.75
988.75	*1,310.00*	(e)	25.00
		(f)	187.50
			321.25

Government Bonds

(f)	187.50		

Office Equipment

	5,000.00		
(b)	300.00		
	5,300.00		

Automobile

	2,100.00		

Accounts Payable

		(b)	300.00

J. D. Knight, Proprietor

			8,000.00

Income from Advertising Fees

		(c)	410.00

Rent Expense

(a)	100.00		

Gas and Electricity

(d)	8.75		

Charitable Contributions

(e)	25.00		

The transactions completed by J. D. Knight are shown recorded in the "T" accounts reproduced in the column at the left. Inasmuch as it is not a complete narrative of transactions for a given period of time, the dates are not specified. The debit and credit amounts are simply entered in "T" accounts to illustrate the application of the debit and credit theory.

The total of the amounts entered on either side of an account is termed a *footing.* When amounts have been entered on both sides of an account, the difference between the footings represents the *balance* of the account. When the footing of the left or debit side of an account is greater than the footing of the right or credit side, the account has a *debit balance.* When the footing of the right or credit side is greater, the account has a *credit balance.* When the footings of both sides are equal, the account is in balance. The footings and the balance of an account should be written in small pencil figures as shown in the cash account. (See amounts in italics.)

Accounts with debit balances represent either assets or expenses. Accounts with credit balances represent either liabilities, capital, or income. The asset accounts will be recognized as those representing property owned. The liability accounts will be recognized as those representing debts owed. The account with J. D. Knight, Proprietor is his capital or permanent proprietorship account. All expense and income accounts are temporary proprietorship accounts.

TRIAL BALANCE OF J. D. KNIGHT

Cash	988	75		
Government Bonds	187	50		
Office Equipment	5,300	00		
Automobile	2,100	00		
Accounts Payable			300	00
J. D. Knight, Proprietor			8,000	00
Income from Advertising Fees			410	00
Rent Expense	100	00		
Gas and Electricity	8	75		
Charitable Contributions	25	00		
	8,710	00	8,710	00

Trial Balance. At the time of opening the accounts for Mr. Knight, the sum of his assets was equal to his proprietorship. In recording each transaction completed thereafter, a double entry was made debiting one account and crediting another account for the same amount. It is evident, therefore, that the sum of the debit entries should be equal to the sum of the credit entries. It is also evident that the sum of the debit and credit balances of the accounts should be equal. This equality is a fundamental characteristic of the double-entry system of bookkeeping. To prove the equality of the account balances it is only necessary to list the balances in parallel columns and to total the columns as shown in the above illustration. This procedure is known as taking a *trial balance.* The accounts shown on page 23 provided the information needed in taking this trial balance.

Analysis of Accounts. The net effect of the transactions completed during an accounting period may be ascertained in either of the following ways:

(a) By an analysis of the asset and liability accounts.
(b) By an analysis of the income and expense accounts.

Mr. Knight's trial balance shows that he owns the following assets:

Cash	$ 988.75
Government Bonds	187.50
Office Equipment	5,300.00
Automobile	2,100.00
Total Assets	$8,576.25

His only liability consists of accounts payable amounting to $300. Since the amounts of his assets and his liabilities are known, the amount of his proprietorship may be ascertained by subtraction ($8,576.25 − $300 = $8,276.25). After ascertaining the amount of the proprietorship the three accounting elements may be expressed in equation form as follows:

ASSETS $8,576.25 = LIABILITIES $300 + PROPRIETORSHIP $8,276.25

Balance Sheet. It is customary to itemize the assets, the liabilities, and the proprietorship in the form of a financial statement that is commonly known as a *balance sheet.* Such a statement prepared for Mr. Knight on the basis of information given in the foregoing analysis would appear as follows:

BALANCE SHEET OF J. D. KNIGHT

ASSETS			LIABILITIES		
Cash	988	75	Accounts Payable	300	00
Government Bonds	187	50			
Office Equipment	5,300	00	PROPRIETORSHIP		
Automobile	2,100	00	J. D. Knight, Proprietor	8,276	25
Total Assets	8,576	25	Total Liabilities and Proprietorship	8,576	25

A comparison of the balance sheet with the accounting equation will reveal a similarity in the manner of listing the assets, the liabilities, and the proprietorship. For example, the assets are listed in the column at the left, while the liabilities and the proprietorship are listed in the column at the right. It will also be noted that the total of the assets is equal to the sum of the liabilities and the proprietorship. The equality of the elements is the reason why the statement is known as a balance sheet.

By comparing the proprietorship at the end of the period with the proprietorship at the beginning of the period, the net increase in the proprietorship may be ascertained.

Proprietorship at end of period	$8,276.25
Proprietorship at beginning of period	8,000.00
Net increase in proprietorship during period	$ 276.25

It will be observed that the transactions completed during the period had the effect of increasing the assets from $8,000 to $8,576.25, the total increase amounting to $576.25. The increase in assets, however, is partially offset by a liability amounting to $300 that was incurred during the period. This liability must be subtracted from the total increase in assets in order to ascertain the net increase in proprietorship ($576.25 − $300 = $276.25).

Profit and Loss Statement. The amount of the net increase in Mr. Knight's proprietorship during the period may also be ascertained by subtracting the sum of the expenses incurred during the period from the total income for the period. His trial balance shows that his income for the period amounted to $410. His expenses for the period consisted of the following:

Rent Expense	$100.00
Gas and Electricity	8.75
Charitable Contributions	25.00
Total Expenses	$133.75

It is customary to itemize the income and the expenses in the form of a financial statement that is commonly known as a *profit and loss statement.* Such a statement prepared for Mr. Knight would appear as follows:

PROFIT AND LOSS STATEMENT OF J. D. KNIGHT

Income:		
Income from Advertising Fees	410 00	
Total Income		410 00
Expenses:		
Rent Expense	100 00	
Gas and Electricity	8 75	
Charitable Contributions	25 00	
Total Expenses		133 75
Net Income		276 25

When the total income for the period exceeds the total expenses for the period, the difference represents the net increase in proprietorship for the period. This net increase is usually referred to as the *net income.* If, on the other hand, the total expenses for the period exceed the total income for the period, the difference represents a net decrease in proprietorship. This net decrease is usually referred to as a *net loss.* By subtracting the amount of the net loss for the period from the amount of the proprietorship at the beginning of the period, the proprietorship at the end of the period may be ascertained.

The balance sheet and the profit and loss statement are *financial statements* that should be prepared at the close of each accounting period. The purpose of the balance sheet is to show the financial condition of the business at the close of the period. The purpose of the profit and loss statement is to show the results of operations during the period.

PRACTICE ASSIGNMENT No. 2. Refer to the workbook and complete Report No. 2 in accordance with the instructions given therein. The work involved in completing the assignment requires a knowledge of the principles developed in the preceding discussion. Any difficulty experienced in completing the practice assignment will indicate a lack of understanding of these principles. In such event further study should be helpful. After completing the report, continue with the following study assignment until the next report is required.

III ACCOUNTING PROCEDURE

In recording the financial transactions or operations of an individual, an organization, or an enterprise, it is customary to keep two types of records as follows:

(a) The original record.
(b) The final record.

The Original Record. As transactions are completed, it is necessary to analyze them in order to determine their effect upon the accounting elements and to make a written record of them in chronological order. Such a record is commonly referred to as a *journal* and the process of recording the transactions therein is referred to as *journalizing.* A journal may be either a bound book or a loose-leaf book. In either case it is customary to number the pages consecutively.

Standard Journal Form. Although the ruling may vary considerably, a journal is generally ruled to facilitate the recording of certain fundamental facts, such as the following:

(a) The date of each transaction.
(b) The titles of the accounts affected by each transaction.
(c) The amount of each transaction.
(d) A description of each transaction.

The ruling of a journal should not only facilitate the recording of the essential information, but should also be an aid in analyzing each transaction and in recording its effect on the accounting elements.

A simple form of journal is the two-column journal shown in Illustration No. 1. The columns have been numbered in this illustration as a means of identification in connection with the following discussion:

Column No. 1 is a date column. It is a double column, the perpendicular single rule being used to separate the month from the day. Thus in writing June 20, the name of the month should be written to the left of the single line and the number representing the day of the month should be written to the right of the single line. The year should be written in small figures at the top of the Date column immediately below the heading and should be repeated at the top of each page and whenever there is a change in the year.

Column No. 2 is generally referred to as a description or an explanation column. It is used to record the titles of the accounts affected by each transaction, together with a description of the transaction. Two or more accounts are affected by each transaction, and the titles of all accounts affected must be recorded. One line should be used to record the title of each account affected regardless of whether the account is to be debited or credited. The titles of the accounts to be debited are generally written to the extreme left of the column, while the titles of the accounts to be credited are usually indented about one-half inch. The description should be written immediately following the debit and credit entries. The description is usually indented about one inch. Reference to the journal reproduced on pages 32 and 33 will help to visualize the arrangement of the copy in the Description column. An orderly arrangement is desirable.

Column No. 3 is a posting reference column — sometimes referred to as a folio column. No entries are made in this column at the time of journalizing the transactions; such entries are made only at the time of posting. This will be explained in detail later.

Column No. 4 is an amount column in which the amount that is to be debited to any account should be written on the line on which the title of the account appears. In other words, the name of the account to be debited should be written in the Description column and the amount of the debit entry should be written in the left-hand amount column.

Column No. 5 is an amount column in which the amount that is to be credited to any account should be written on the line on which the title of the account appears. In other words, the name of the account to be credited should be written in the Description column and the amount of the credit entry should be written in the right-hand amount column.

JOURNAL

DATE	DESCRIPTION	POST. REF.	DEBITS	CREDITS
1	2	3	4	5

Illustration No. 1, Standard Two-Column Journal

Journalizing. Journalizing involves recording the desired information concerning each transaction either (a) at the time the transaction occurs or (b) subsequently, but in the order in which the transactions occur, that is to say, chronologically. In every entry it is essential to record the date of each transaction, the titles of the accounts affected by each transaction, the amount of each transaction, and a brief description of each transaction. Furthermore, the effect of each transaction upon the accounts should be indicated. The only effect a transaction can have on any account is either to increase or to decrease the amount of the account. Before a transaction can be recorded properly, therefore, it must be analyzed in order to determine the following information:

(a) What accounts are affected by the transaction.
(b) What effect the transaction has upon each of the accounts.
(c) How the effect upon the accounts may be recorded.

When it is known what accounts are being kept and when the effect upon the accounts has been determined by analysis, recording a transaction is a relatively simple matter.

Journal Illustrated. The procedure in journalizing transactions is illustrated by reproducing the journal of J. D. Knight, who is the proprietor of an advertising agency. A *narrative of transactions* is a statement of information giving the essential facts regarding transactions for recording purposes.

The narrative of transactions completed by Mr. Knight during the month of February provides all the information that is needed in journalizing the transactions. Mr. Knight's journal is reproduced on pages 32 and 33.

NARRATIVE OF TRANSACTIONS

J. D. Knight, Proprietor

Tuesday, February 1

Paid office rent for February in advance, $100.

Since the effect of this transaction was to increase the amount of rent expense and to decrease the amount of cash, it was recorded in the journal by debiting Rent Expense and by crediting Cash.

Thursday, February 3

Received $120 from the Atlas Dry Cleaning Co. in full payment for services rendered.

Since the amount received from the Atlas Dry Cleaning Co. represented an increase in cash and also an increase in income, it was recorded in the journal by debiting Cash and by crediting Income from Advertising Fees.

Saturday, February 5

Paid telephone bill for January service, $8.75.

This transaction resulted in an increase in expense and a decrease in cash. It was, therefore, recorded in the journal by debiting Telephone and Telegraph Expenses and by crediting Cash.

Monday, February 7

Paid gas and electric bill for January service, $9.50.

The effect of this transaction was the same as in the preceding transaction. It was recorded in the journal by debiting Gas and Electricity and by crediting Cash.

Tuesday, February 8

Received $75 from The City Restaurant in payment for services.

Wednesday, February 9

Paid Whitcomb and Riley $150 on account.

This transaction resulted in a decrease in accounts payable with a corresponding decrease in cash. It was recorded in the journal by debiting Accounts Payable and by crediting Cash.

Thursday, February 10

Paid garage bill covering storage and gas and oil purchases for January, $17.80.

Friday, February 11

Received $140 from The Matthews Manufacturing Co. in payment for advertising service.

Saturday, February 12

Paid $3 for a magazine subscription to *Advertising and Selling*.

Monday, February 14

Received $240 from the Wyatt Coal Sales Co. in payment for services.

Tuesday, February 15

Gave Virginia Conrad $87.50 in payment of her salary for the first half of the month.

Miss Conrad is employed by Mr. Knight as his secretary and bookkeeper at a salary of $175 a month.

Thursday, February 17

Paid $150 for a typewriter to be used in the office.

This transaction had the effect of increasing office equipment and decreasing cash; hence it was recorded by debiting Office Equipment and by crediting Cash.

Friday, February 18

Paid traveling expenses totaling $28.60 while on a business trip out of the city.

Saturday, February 19

Gave the Community Chest $12.

Monday, February 21

Received $80 from Roscoe Chandler in payment for advertising services.

Wednesday, February 23

Paid $25 for membership dues in the National Association of Advertisers.

Thursday, February 24

Purchased a government bond for $37.50.

Friday, February 25

Purchased a filing cabinet for office use from Whitcomb and Riley on credit, $85.

This transaction resulted in an increase in office equipment with a corresponding increase in accounts payable. It was, therefore, recorded in the journal by debiting Office Equipment and by crediting Accounts Payable.

Saturday, February 26

Paid $3.15 for stationery and miscellaneous office supplies.

Monday, February 28

Gave Virginia Conrad $87.50 in payment of her salary for the last half of the month.

Mr. Knight withdrew $150 for personal use.

Amounts withdrawn for personal use by the proprietor of a business enterprise represent a decrease in proprietorship and a corresponding decrease in cash. Such withdrawals should never be recorded in the same account as salaries paid to employees. While amounts withdrawn might be recorded as debits to the proprietor's capital account, it is better practice to record withdrawals in a separate account for the reason that such withdrawals are usually made in anticipation of profits. This transaction was recorded in the journal by debiting J. D. Knight, Drawing, and by crediting Cash.

32 JOURNAL

Date		Description	Post. Ref.	Debits	Credits
19— Feb.	1	Rent Expense	9	100 00	
		Cash	1		100 00
		Paid February rent.			
	3	Cash	1	120 00	
		Income from Advertising Fees	8		120 00
		Atlas Dry Cleaning Co.			
	5	Telephone and Telegraph Exp.	10	8 75	
		Cash	1		8 75
		Paid January telephone bill.			
	7	Gas and Electricity	14	9 50	
		Cash	1		9 50
		Paid gas and electric bill for January.			
	8	Cash	1	75 00	
		Income from Advertising Fees	8		75 00
		The City Restaurant.			
	9	Accounts Payable	5	150 00	
		Cash	1		150 00
		Whitcomb & Riley on account.			
	10	Automobile Expense	12	17 80	
		Cash	1		17 80
		Paid January garage bill.			
	11	Cash	1	140 00	
		Income from Advertising Fees	8		140 00
		The Matthews Mfg. Co			
	12	Miscellaneous Expenses	16	3 00	
		Cash	1		3 00
		Paid for subscription to Advertising and Selling			
	14	Cash	1	240 00	
		Income from Advertising Fees	8		240 00
		Wyatt Coal Sales Co.			
	15	Salaries	11	87 50	
		Cash	1		87 50
		Paid secretary's salary.			
	17	Office Equipment	3	150 00	
		Cash	1		150 00
		Purchased typewriter.			
				1101 55	1101 55

J. D. Knight's Journal

The numbers entered in the Posting Reference column indicate that the posting has been completed. These numbers were not entered at the time of journalizing; they were entered as the posting was completed.

33

Date		Description	Post. Ref.	Debits	Credits
Feb	18	Traveling Expenses	15	28 60	
		Cash	1		28 60
		Paid expenses on business			
		trip out of city.			
	19	Charitable Contributions	17	12 00	
		Cash	1		12 00
		Community Chest.			
	21	Cash	1	80 00	
		Income from Advertising Fees	8		80 00
		Roscoe Chandler.			
	23	Miscellaneous Expenses	16	25 00	
		Cash	1		25 00
		N.A.A dues.			
	24	Government Bonds	2	37 50	
		Cash	1		37 50
		Purchased Bonds.			
	25	Office Equipment	3	85 00	
		Accounts Payable	5		85 00
		Whitcomb & Riley.			
	26	Stationery and Supplies	13	3 15	
		Cash	1		3 15
		Purchased office supplies.			
	28	Salaries	11	87 50	
		Cash	1		87 50
		Paid secretary's salary.			
	28	J. D. Knight, Drawing	7	150 00	
		Cash	1		150 00
		Personal use.		508 75	508 75
				508 75	508 75

J. D. Knight's Journal (Concluded)

Proving the Journal. One of the distinctive features of double-entry bookkeeping is that it provides a means of proof. Because a double entry is made for each transaction that is journalized, the equality of debit and credit entries on each page of the journal may be proved merely by footing the amount columns. The entries made to record the transactions for each day, week, month, or other period may be proved in similar manner. The debits and the credits must always be equal in amount, and proof of equality may be ascertained at any time merely by footing the amount columns to find the total of the debit and credit entries. It is good practice to foot each page of the journal as a means of proof. The footings are usually entered first in small pencil figures. After making sure that the footings of each page are equal in amount, the totals may be recorded in ink as shown on pages 32 and 33. There is no need to carry the totals forward to the end of the month, although this may be done if desired.

The Final Record. Since the transactions are recorded in chronological order in the journal, the entries affecting a particular account are not grouped together; hence there is need for another type of record in which the information appearing in the original record may be summarized to show the status of each account.

The Ledger. A group of accounts constitutes a *ledger*. The use of a ledger makes it possible to summarize the information recorded in the journal and to assort and rearrange the accounts and the data in whatever form is desired. A ledger may be (a) a bound book, (b) a loose-leaf book, or (c) cards kept in a box file.

Standard Account Form. The "T" account form was introduced on page 15 as the simplest form of account that might be used for teaching or for memorandum purposes. A more complete form is required for actual accounting practice. Such a form is shown in Illustration No. 2. This is sometimes referred to as the standard account form. It will also be found listed in the catalogues of various blankbook manufacturers as "regular," "divided," or "double-entry" ledger form. It is the most widely used account form for general ledger purposes. It is arranged to facilitate the recording of the following essential information:

(a) The account title and any other information that may be desired in the heading of the account.

(b) Debits to the account, including (1) the date of each transaction, (2) any desired information regarding each transaction, (3) the folio or page of the journal from which the information has been transferred, and (4) the amount.

(c) Credits to the account, including (1) the date of each transaction, (2) any desired information regarding each transaction, (3) the folio or page of the journal from which the information has been transferred, and (4) the amount.

It will be noted that the form is divided into two equal parts. The debit and the credit sides are ruled identically for convenience in recording the desired information regarding debits and credits. Two check (√) columns are provided, one preceding the debit amount column and the other preceding the credit amount column. These columns are used for checking purposes only.

ACCOUNT

DATE	ITEMS	FOL.	√	DEBITS	DATE	ITEMS	FOL.	√	CREDITS

Illustration No. 2, Standard Account Form

Classification of Accounts. There are three types of accounts; namely, asset, liability, and proprietorship accounts. All accounts may be classified under these three headings. In arranging the accounts in a ledger, it is customary to group them according to class. In other words, the asset accounts are grouped together, the liability accounts together, and the proprietorship accounts together. A proper grouping of the accounts in the ledger is an aid in preparing the various reports required by the management.

Before any transactions are recorded, it is necessary to determine what accounts should be kept. The accounts to be kept depend upon the information needed or desired. Ordinarily it will be found desirable to keep a separate account with each type of asset and each type of liability. Obviously, information will be desired in regard to what is owned and what is owed. A permanent proprietorship or capital account should be kept in order that information may be available as to the proprietor's investment in the business. Furthermore, it is advisable to keep separate accounts with each type of income and each kind of expense. These are the temporary accounts that are used in recording increases and decreases in proprietorship. The specific accounts to be kept in recording the increases and the decreases in proprietorship depend upon the nature and the sources of the income and of the expenses incurred in earning the income.

A professional man or an individual engaged in operating a small business may need to keep relatively few accounts to record the information that he needs or in which he is interested. On the other hand, a large manufacturing enterprise, a public utility, or any large business may need to keep a great many accounts in order that the information required or desired may be available. Regardless of the number of accounts kept, they can be segregated into the three general classes, and they should be grouped according to these classes in the ledger. The usual custom is to arrange the asset accounts first, the liability accounts second, and the proprietorship accounts, including the income and the expense accounts, last. This procedure, however, is not uniform and some variation may be expected in actual practice.

Chart of Accounts. A *chart of accounts* is a properly classified list of accounts that serves as a guide to the bookkeeper in recording the transactions. In establishing a system of accounts, the first step is to prepare a chart of the accounts to be kept. The preparation of a chart of accounts involves the following:

(a) Determining what specific accounts are required.
(b) Selecting appropriate titles for the accounts.

Each account should be given a title that will indicate the nature of the information recorded therein. A chart of the accounts used by J. D. Knight in recording his transactions follows:

CHART OF ACCOUNTS FOR J. D. KNIGHT

*Assets**
Cash
Government Bonds
Office Equipment
Automobile

Liabilities
Accounts Payable

Proprietorship
J. D. Knight, Proprietor
J. D. Knight, Drawing

Income
Income from Advertising Fees

Expenses
Rent Expense
Telephone and Telegraph Expense
Salaries
Automobile Expense
Stationery and Supplies
Gas and Electricity
Traveling Expenses
Miscellaneous Expenses
Charitable Contributions

**Headings are set in italics to distinguish from account titles.*

Opening the Ledger. Before any posting can be completed, it is necessary to open the accounts by inserting the proper headings and recording the beginning balances. The chart of accounts and the trial balance are usually the sources of the information needed in opening the ledger accounts. The chart of accounts provides the titles of the accounts and indicates the order in which they should be kept in the ledger. The trial balance provides the amounts of the beginning balances.

Mr. Knight's ledger is reproduced on pages 39 to 41. His trial balance, reproduced on page 24, provided the amounts of the beginning balances and indicated whether they were debit or credit balances. In entering the balance of each account, the date was written in the Date column, the word "Balance" in the Items column, and the amount in the Debits or Credits column, depending upon whether the balance was a debit or a credit balance. Some of the accounts had no beginning balances, but they were included when the ledger was opened because the chart of accounts indicated that they would be needed later.

Inasmuch as Mr. Knight makes but few purchases on credit, he does not keep a separate ledger account for each creditor. When invoices are received for items purchased on credit, the invoices are checked and recorded in the journal by debiting the proper accounts and by crediting Accounts Payable. Accounts Payable is a summary account, the balance of which is a liability representing the total amount due to creditors. After each invoice is recorded, it is filed in an unpaid invoice file, where it remains until it is paid in full. When an invoice is paid in full, it is removed from the unpaid invoice file and is then filed under the name of the creditor for future reference. The balance of the accounts payable summary account may be proved at any time by ascertaining the total of the unpaid amounts of the invoices.

Posting. The process of recording information in the ledger is known as *posting*. All amounts entered in the journal should be posted to the accounts kept in the ledger in order to summarize the results. Such posting may be done daily or at frequent intervals. The ledger is not a reliable source of information until all the transactions recorded in the books of original entry have been posted.

Since the accounts provide the information needed in preparing accounting reports, a posting procedure that will insure accuracy in maintaining the accounts must necessarily be followed. Posting from the journal to the ledger involves recording the following information in the accounts:

(a) The date of each transaction.

(b) The amount of each transaction.

(c) The page or folio of the journal from which each transaction is posted.

As each entry in the journal is posted to the proper account in the ledger, the page of the ledger on which the account appears should be entered in the Posting Reference column of the journal so as to provide a cross reference between the journal and the ledger.

It will be seen from the foregoing discussion that there are four steps involved in posting — three involving information to be recorded in the ledger and one involving information to be recorded in the journal. The date, the amount, and the effect of each transaction are recorded in the journal. The same information is later posted to the ledger. Posting does not involve an analysis of each transaction to determine its effect upon the accounts. Such an analysis is made at the time of recording the transaction in the journal, and posting is merely transferring the information from the journal to the ledger. In posting, care should be used to record each debit and each credit entry in the proper columns so that the entries will correctly reflect the effect of the transaction on the accounts.

When the posting is completed, the same information is provided in both the journal and the ledger as to the date, the amount, and the effect of each transaction. A cross reference from each book to the other book is also provided. This cross reference makes it possible to trace the entry of February 1 on the credit side of the cash account in the ledger to the journal by referring to the page indicated in the Folio column. The entry of February 1 on the debit side of the rent expense account may also be traced to the journal by referring to the page indicated in the Folio column. Each entry in the journal may be traced to the ledger by referring to the page numbers indicated in the Posting Reference column of the journal. By referring to pages 32 and 33, it will be seen that the ledger folios were inserted in the Posting Reference column. This was done as the posting was completed.

In posting, care should be used in writing the date as well as the amount of each entry. The year should be written at the top of the Date column and need not be repeated so long as it does not change. The name of the month should be written in the left-hand Date column and the day of the month should be written in the right-hand Date column. The proper abbreviation may be used for the month and it need not be repeated for su' sequent entries during the same month.

(Continued on page 42)

LEDGER

ACCOUNT *Cash* *Page 1*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb.	1	Balance	✓		988 75	19— Feb.	1		32		100 00
	3		32		120 00		5		32		8 75
	8		32		75 00		7		32		9 50
	11		32		140 00		9		32		150 00
	14		32		240 00		10		32		17 80
	21		33		80 00		12		32		3 00
		773.45			1,643 75		15		32		87 50
							17		32		150 00
							18		33		28 60
							19		33		12 00
							23		33		25 00
							24		33		37 50
							26		33		3 15
							28		33		87 50
							28		33		150 00
											[illegible]

ACCOUNT *Government Bonds* *Page 2*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb.	1	Balance	✓		187 50						
	24		33		37 50						
					225 00						

ACCOUNT *Office Equipment* *Page 3*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb.	1	Balance	✓		5300 00						
	17		32		150 00						
	25		33		85 00						
					5535 00						

ACCOUNT *Automobile* *Page 4*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
Feb.	1	Balance	✓		2100 00						

J. D. Knight's Ledger

ACCOUNT *Accounts Payable* Page 5

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb	9		32		150 00	19— Feb	1	Balance	✓		300 00
							25	235.00	33		85 00
											385 00

ACCOUNT *J. D. Knight, Proprietor* Page 6

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Feb	1	Balance	✓		8000 00

ACCOUNT *J. D. Knight, Drawing* Page 7

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb	28		33		150 00						

ACCOUNT *Income from Advertising Fees* Page 8

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Feb	1	Balance	✓		410 00
							3		32		120 00
							8		32		75 00
							11		32		140 00
							14		32		240 00
							21		33		80 00
											1065 00

ACCOUNT *Rent Expense* Page 9

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb	1	Balance	✓		100 00						
	1		32		100 00						
					200 00						

ACCOUNT *Telephone and Telegraph Expense* Page 10

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Feb	5		32		8 75						

J. D. Knight's Ledger (Continued)

ACCOUNT *Salaries* Page 11

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	15		32		87 50					
	28		33		87 50					
					175 00					

ACCOUNT *Automobile Expense* Page 12

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	10		32		17 80					

ACCOUNT *Stationery and Supplies* Page 13

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	26		33		3 15					

ACCOUNT *Gas and Electricity* Page 14

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	1	Balance	✓		8 75					
	7		32		9 50					
					18 25					

ACCOUNT *Traveling Expenses* Page 15

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	18		33		28 60					

ACCOUNT *Miscellaneous Expenses* Page 16

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	12		32		3 00					
	23		33		25 00					
					28 00					

ACCOUNT *Charitable Contributions* Page 17

Date		Items	Folio	✓	Debits	Date	Items	Folio	✓	Credits
19— Feb.	1	Balance	✓		25 00					
	19		33		12 00					
					37 00					

J. D. Knight's Ledger (Concluded)

The ledger of J. D. Knight is shown after posting from the journal was completed. The accounts are arranged in the same order in which they appear in the chart of accounts shown on page 36. Each account was kept on a separate page of the ledger and the pages were numbered consecutively. Before posting the February transactions, the balances of the accounts as of February 1 were entered. This information was obtained from the trial balance reproduced on page 24.

The Trial Balance. The purpose of a trial balance is to prove the equality of debit and credit balances. In double-entry bookkeeping, equality of debit and credit balances in the ledger must be maintained. Proof of this equality is obtained periodically by means of a trial balance. A trial balance may be taken daily, weekly, monthly, or whenever desired. Before taking a trial balance, all transactions previously completed should be journalized and the posting should be completed in order that the effect of all transactions may be reflected in the ledger accounts.

Footing Accounts. When a form of ledger account similar to the one in Illustration No. 2 is used, it is necessary to foot or add the amounts recorded in each account preparatory to taking a trial balance. The footings should be recorded in small pencil figures immediately below the last item in both the debit and the credit amount columns of the account. At the same time the difference between the footings, that is, the balance, should be recorded in small pencil figures in the Items column of the account on the side of which the footing is the greater. In other words, if an account has a debit balance, the balance should be written in the Items column on the debit or left-hand side of the account; if the account has a credit balance, the balance should be written in the Items column on the credit or right-hand side of the account. The balance or difference between the footings should be recorded in the Items column just below the line on which the last regular entry appears and in line with the footing.

Reference to the accounts kept in the ledger shown on pages 39 to 41 will reveal that the accounts have been footed and will show how the footings and the balances are recorded. Of course, when only one item has been posted to an account, regardless of whether it is a debit or a credit amount, no footing is necessary.

Care should be used in ascertaining the balances of the accounts. If an error is made in adding the columns or in determining the difference between the footings, the error will be reflected in the trial balance, and considerable time may be required to locate it. Most accounting errors result from carelessness. For example, a careless bookkeeper may write an account balance on the wrong side of an account or may enter figures so illegibly that they may be misread later. Neatness in writing the amounts is just as important as carefulness in determining the footings and the balances. The footings of an account should be written in small pencil figures close to the preceding line so that they will not interfere with the recording of an item on the next ruled line.

Proving the Balances of the Accounts. To prove the balances of the accounts, it is customary to list all of the open accounts in the same order in which they appear in the ledger. The accounts should be kept in the ledger in proper order so that it will not be necessary to rearrange them in listing them for the purpose of a trial balance. If the accounts are not listed in proper order in the trial balance, some confusion in preparing the accounting reports may result.

It is important that the following procedure should be observed in preparing a trial balance:

(a) Head the trial balance, being sure to give the name of the individual, firm, or organization and the date as of which the trial balance is being taken.

(b) List the account titles in the proper order, showing the page number of the ledger on which each account appears.

(c) Record the account balances in parallel columns, entering debit balances in the left-hand column and credit balances in the right-hand column.

(d) Foot the columns and record the totals, ruling a single line across the amount columns above the totals and a double line below the totals.

If the footings of the trial balance are equal in amount, the equality indicates that the ledger is in balance. In other words, the equality of the footings of the trial balance is an indication that the equality of the debit and the credit amounts has been maintained, not only in journalizing the transactions, but also in posting from the journal to the ledger and in listing the open account balances in the trial balance.

The information given in the trial balance reproduced on page 44 was obtained from the ledger of J. D. Knight reproduced on pages 39 to 41.

A trial balance may be typewritten on unruled paper, or it may be penwritten on two-column journal ruled paper. The following trial balance is reproduced from penwritten copy on journal ruled paper.

J. D. Knight
Trial Balance, February 28, 19–

Accounts	Page	Dr. Balances	Cr. Balances
Cash	1	773 45	
Government Bonds	2	225 00	
Office Equipment	3	5535 00	
Automobile	4	2100 00	
Accounts Payable	5		235 00
J. D. Knight, Proprietor	6		8000 00
J. D. Knight, Drawing	7	150 00	
Income from Advertising Fees	8		1065 00
Rent Expense	9	200 00	
Telephone and Telegraph Expense	10	8 75	
Salaries	11	175 00	
Automobile Expense	12	17 80	
Stationery and Supplies	13	3 15	
Gas and Electricity	14	18 25	
Traveling Expenses	15	28 60	
Miscellaneous Expenses	16	28 00	
Charitable Contributions	17	37 00	
		9300 00	9300 00

J. D. Knight's Trial Balance

PRACTICE ASSIGNMENT No. 3. Refer to the workbook and complete Report No. 3 in accordance with the instructions given therein. If any difficulty is encountered in completing this assignment, it is an indication that the principles developed in Unit One have not been thoroughly mastered; hence this unit should be reviewed. It is important that Unit One be thoroughly mastered before proceeding with Unit Two.

Unit Two

ACCOUNTING FOR MERCHANDISE

IV THE MERCHANDISE ACCOUNTS

One of the principal divisions of business activity is that of merchandising, that is, buying and selling goods. In this field the retail merchant and the wholesale merchant are important factors. A *retail merchant* is one who sells to the consumer at retail prices. He may buy direct from manufacturers, producers, or importers, or he may buy from jobbers, distributors, or other middlemen at wholesale prices. A *wholesale merchant* is one who sells to retail merchants and large consumers at wholesale prices. He usually buys from the manufacturers, producers, or importers. Thus a wholesale firm may buy merchandise from various manufacturers, producers, or importers and sell it at wholesale prices to retail dealers who in turn sell to their customers at retail prices.

The retail merchandising business is a broad field of endeavor including such enterprises as grocery and food stores, clothing and dry goods stores, household furniture and furnishings stores, drug stores, hardware and equipment stores, department stores, and many other types of retail stores.

Anyone engaged in a mercantile enterprise must keep records, not only because federal and state laws require it, but in order to operate his business intelligently. Sales should be recorded as income in the period in which the merchandise is sold. However, all of the income from sales does not represent profit. The cost of the goods sold must be taken into consideration in computing the gross profit on sales, and the operating expenses must be taken into consideration in computing the net profit on sales.

In ascertaining the cost of goods sold, it is necessary to take into consideration (a) the amount of any goods on hand at the beginning of the period, (b) the amount of goods purchased during the period, (c) the amount of any goods returned to creditors or suppliers or any allowances received from creditors during the period that resulted in a decrease in the cost of the goods purchased, and (d) the amount of any goods on hand at the end of the period.

To be successful, a merchant should have sufficient capital to acquire the necessary equipment and a stock of merchandise. He should also be able to pay all of his operating expenses and to realize a reasonable profit on the amount of capital invested in the enterprise. Adequate records may not prevent a merchant from failing, but they will undoubtedly increase his chances of succeeding.

In recording transactions arising from merchandising, it is desirable to keep at least the following accounts:

(a) Merchandise Inventory
(b) Purchases
(c) Purchases Returns and Allowances
(d) Sales
(e) Sales Returns and Allowances

Merchandise Inventory Account. A merchandise inventory account is an asset account in which the cost of goods in stock at the time of taking an inventory is recorded. It is customary to take an inventory of merchandise in stock at the close of each accounting period. The amount of the inventory is then recorded as a debit to Merchandise Inventory. The amount debited to the inventory account at the close of one accounting period also represents the amount of the inventory at the beginning of the succeeding accounting period. In other words, an inventory taken on December 31 of the calendar year represents the inventory both at the close of an old year and at the beginning of a new year.

MERCHANDISE INVENTORY

Debit to record inventory of goods in stock	

Purchases Account. The purchases account is a temporary account in which the cost of merchandise purchased is recorded. The account should be debited for the cost of all merchandise purchased during the accounting period, whether for cash or on credit. It may also be debited for any transportation charges, such as freight, express, and parcel post charges, that increase the cost of the merchandise purchased.

PURCHASES

Debit to record the cost of merchandise purchased	

Purchases Returns and Allowances Account. This account is a temporary account in which purchases returns and allowances are recorded. The account should be credited for the cost of any merchandise returned to creditors or suppliers and for any allowances received from creditors that decrease the cost of the merchandise purchased. Allowances may be received from creditors for merchandise delivered in poor condition or for merchandise that does not meet specifications as to quality, weight, size, color, grade, style, etc.

PURCHASES RETURNS AND ALLOWANCES	
	Credit to record returns and allowances

Purchase Invoice. The source of the information needed in recording a purchase transaction is the *purchase invoice.* A standard purchase invoice form has been widely adopted by merchants, manufacturers, distributors, and other users. It was originally developed by the National Association of Purchasing Agents in collaboration with the Railway Accounting Officers Association, the National Association of Cost Account-

INVOICE
IMPERIAL FURNITURE COMPANY
GRAND RAPIDS, MICHIGAN

CUSTOMER'S ORDER NO. & DATE 196
REQUISITION NO.
CONTRACT NO.
REFER TO INVOICE NO. 14251
INVOICE DATE Dec. 2, 19--
VENDOR'S NOS.

SOLD TO W. L. Mann
12 N. Third Street
Cincinnati, Ohio

SHIPPED TO AND DESTINATION W. L. Mann
12 N. Third Street
Cincinnati, Ohio

DATE SHIPPED Dec. 2, 19-- FROM Grand Rapids PREPAID OR COLLECT?
CAR INITIALS AND NO. F. O. B. Grand Rapids
HOW SHIPPED AND ROUTE Pa. R. R.
TERMS 3/10,n/30

FOR CUSTOMER'S USE ONLY
REGISTER NO. | VOUCHER NO.
F. O B CHECKED
TERMS APPROVED W. S. | PRICE APPROVED W. S.
CALCULATIONS CHECKED R. M.
TRANSPORTATION
FREIGHT BILL NO. | AMOUNT
MATERIAL RECEIVED 12/5 19-- H. T. R. C.
DATE SIGNATURE TITLE
SATISFACTORY AND APPROVED
ADJUSTMENTS
ACCOUNTING DISTRIBUTION
AUDITED B. M. | FINAL APPROVAL J. F. S.

QUANTITY ORDERED	QUANTITY SHIPPED	DESCRIPTION	UNIT PRICE	AMOUNT
1	1	4119 Mhg. Tier Table	11.50	11.50
2	2	662 Mhg. Occasional Table	10.50	21.00
1	1	635 Mhg. Occasional Table	15.50	15.50
1	1	2630 Mhg. Night Stand	12.50	12.50
3	3	2317 Mhg. Coffee Table	9.75	29.25
				89.75

Illustration No. 3, Purchase Invoice

ants, and the Association of American Railroads. The standard form has been approved by the Division of Simplified Practice of the National Bureau of Standards, U. S. Department of Commerce. The size of the form approved is 8½″ wide by 7″, 11″, or 14″ long. As indicated, the length may vary according to needs. The purchase invoice shown in Illustration No. 3 was prepared on a standard invoice form.

Merchandise may be bought for cash or on credit. When merchandise is bought for cash, the transaction results in an increase in purchases and a decrease in the asset cash; hence it should be recorded by debiting Purchases and by crediting Cash. When merchandise is bought on credit, the transaction results in an increase in purchases with a corresponding increase in the liability accounts payable; hence it should be recorded by debiting Purchases and by crediting Accounts Payable.

Accounts Payable. In order that the proprietor may know the total amount owed to his creditors at any time, it is advisable to keep a summary ledger account with Accounts Payable. This is a liability account. The credit balance of the account at the beginning of the period represents the total amount owed to creditors. During the period, the account should be credited for the amount of any transactions involving increases and should be debited for the amount of any transactions involving decreases in the amount owed to creditors. At the end of the period, the credit balance of the account again represents the total amount owed to creditors.

It is also necessary to keep some record of the transactions completed with each creditor in order that information may be readily available at all times as to the amount owed to each creditor and as to when each invoice should be paid. The following methods of accounting for credit purchases are widely used:

(*a*) ***The invoice method.*** Under this method it is customary to keep a chronological record of the purchase invoices received and to file them systematically. All other vouchers or documents representing transactions completed with creditors should be filed with the purchase invoices. Special filing equipment facilitates the use of this method.

(*b*) ***The ledger account method.*** Under this method it is customary to keep a chronological record of the purchase invoices received. An individual ledger account with each creditor is also kept. Special equipment may be used in maintaining a permanent file of the invoices and other vouchers or documents supporting the records.

Purchases Journal. All of the transactions of a mercantile enterprise can be recorded in an ordinary two-column general journal. In a mercantile enterprise purchase transactions occur frequently. In a business where the proprietor follows the practice of purchasing most of his merchandise on credit, such transactions may be recorded in a special journal advantageously. One form of *purchases journal* is illustrated below. The following transactions, representing purchases of merchandise on credit by P. A. Mosely, a retail merchant, during the month of May, are shown recorded in the illustration:

May 2. Dobson Bros., Dayton; $778.92; Invoice No. 23 dated May 2; terms, 30 days.

6. A. W. Shaw Co., City; $386.50; Invoice No. 24 dated May 5; terms, 30 days.

12. Gray Mfg. Co., 420 Spring Street, City; $1,203.60; Invoice No. 25 dated May 12; terms, 10 days.

29. Dobson Bros.; $1,398.60; Invoice No. 26 dated May 27; terms, 60 days.

PURCHASES JOURNAL FOR MONTH OF May 19— 49

DATE OF ENTRY		DATE OF INVOICE		NO. OF INVOICE	FROM WHOM PURCHASED	POST. REF.	AMOUNT		DATE PAID
					AMOUNT FORWARDED				
May	2	May	2	23	Dobson Bros.	✓	778	92	
	6		5	24	A. W. Shaw Co.	✓	386	50	
	12		12	25	Gray Mfg. Co.	✓	1203	60	
	29		27	26	Dobson Bros	✓	1398	60	
							3767	62	
	31				Purchases Dr.-Accounts Payable Cr.	40/26	3767	62	

Purchases Journal

It will be noted that in recording each invoice, the following information was entered in the purchases journal:

(a) Date on which the invoice is recorded.
(b) Date of the invoice.
(c) Number of the invoice.
(d) From whom purchased (the creditor).
(e) Amount of the invoice.
(f) Date paid.

With this form of purchases journal, each transaction can be recorded on one horizontal line. As purchase invoices are received, it is customary to number them consecutively. This number should not be confused with the order number or the vendor's number, both of which are usually shown on each purchase invoice.

If an individual ledger account is not kept with each creditor, the purchase invoices should be filed immediately after they have been recorded in the purchases journal. It is preferable that they be filed according to due date in an unpaid invoice file.

If a partial payment is made on an invoice, a notation of the payment should be made on the invoice, which should be retained in the unpaid invoice file until it is paid in full. It is generally considered a better policy to pay each invoice in full. Paying specific invoices in full simplifies record keeping for both the buyer and the seller. If credit is received because of returns or allowances, a notation of the amount of the credit should also be made on the invoice so that the balance due will be indicated.

When an invoice is paid in full, the date of payment should be entered in the purchases journal in the column provided for this purpose. The payment should also be noted on the invoice, which should be transferred from the unpaid invoice file to a paid invoice file.

The unpaid invoice file is usually arranged with a division for each month with folders numbered 1 to 31 in each division. This makes it possible to file the unpaid invoices according to the date they will become due, which facilitates payment of the invoices on or before their due dates. Since certain invoices may be subject to discounts if paid within a specified time, it is important that they be handled in such a manner that payment in time to get the benefit of the discounts will not be overlooked.

The folders in the paid invoice file are usually arranged in alphabetic order, according to the names of creditors. This facilitates the filing of all paid invoices, and all other vouchers or documents representing transactions with creditors, in such a manner that a complete history of the business done with each creditor is maintained.

Posting from the Purchases Journal. Under the invoice method of accounting for credit purchases, individual posting from the purchases journal is not required. When this plan is followed, it is customary to place a check mark in the Posting Reference column of the purchases journal at the time of entering each invoice.

At the end of the month the Amount column of the purchases journal should be footed, the total recorded, and the ruling completed as illustrated. The total credit purchases for the month should then be posted as a debit to Purchases and as a credit to Accounts Payable. When posting this item, it is advisable to write "Total Cr. purchases" in the Items column of the accounts with Purchases and Accounts Payable. The titles of both accounts and the posting references may be entered on one horizontal line of the purchases journal as shown in the illustration. Posting the total in this manner is usually referred to as *summary posting.*

Under this plan of accounting, the proprietor need only refer to the accounts payable account to ascertain the total amount owed to his creditors at any time. The balance of the account may be proved by ascertaining the total of the unpaid balances of the invoices kept in the unpaid invoice file.

Schedule of Accounts Payable. It is usually advisable at the end of each month to prepare a list of the creditors showing the name of each creditor and the amount due him. This is known as a *schedule of accounts payable.* Such a schedule can be prepared easily by going through the unpaid invoice file and listing the names of the creditors and the amount due to each. Should the total of the schedule not be in agreement with the balance of the summary account with Accounts Payable, it is an indication that an error has been made either in recording the transactions with creditors in the summary account with Accounts Payable or in handling the invoices. If the error is in the summary account, it will usually be revealed by the trial balance. If the trial balance reveals that the debit and the credit balances are equal in amount, it will indicate that the error has probably been made in handling the invoices.

If an individual ledger account is kept with each creditor, all transactions representing either increases or decreases in the amount owed to each creditor should be posted individually to the proper account. The posting may be done by hand or posting machines may be used. If the posting is done by hand, it may be completed either direct from the purchase invoices and other vouchers or documents representing the transactions, or it may be completed from the books of original entry. If the posting is done with the aid of posting machines, it will usually be completed direct from the purchase invoices and other vouchers or documents. The ledger account method of accounting for accounts payable is explained in detail in a subsequent unit.

Sales Account. The sales account is a temporary account in which the income resulting from sales of merchandise is recorded. The account should be credited for the selling price of all merchandise sold during the accounting period, whether for cash or on credit.

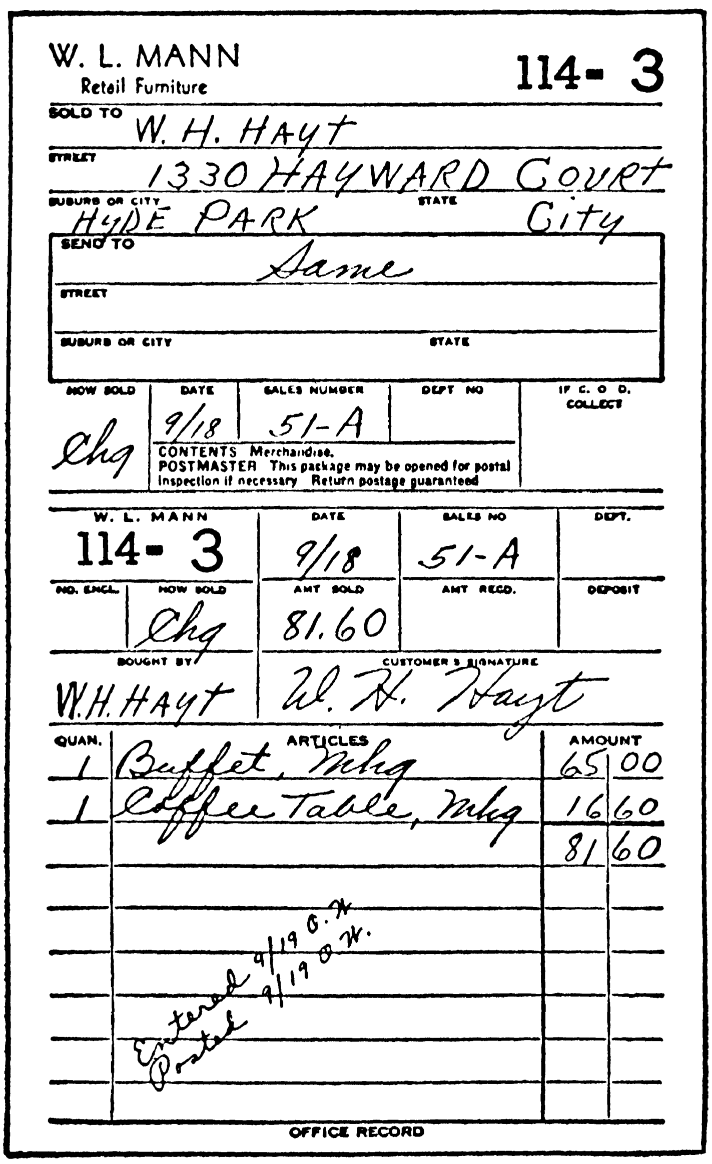
SALES

	Credit to record the selling price of merchandise sold

Sales Returns and Allowances Account. This account is a temporary account in which sales returns and allowances are recorded. The account should be debited for the selling price of any merchandise returned by customers or for any allowances made to customers that decrease the selling price of the merchandise sold. Such allowances may be granted to customers for merchandise delivered in poor condition or for merchandise that does not meet specifications as to quality, weight, size, color, grade, style, etc.

SALES RETURNS AND ALLOWANCES	
Debit to record returns and allowances	

Sales Ticket. The original record of a sales transaction is the sales ticket. Whether merchandise is sold for cash or on credit, a sales ticket should be prepared. When the sale is for cash, the ticket may be printed by the cash register at the time the sale is rung up. However, some stores prefer to use handwritten sales tickets regardless of whether the sale is for cash or on credit. Regardless of the method used in recording cash


W. L. MANN
Retail Furniture
114- 3

SOLD TO W. H. Hayt
STREET 1330 Hayward Court
SUBURB OR CITY Hyde Park STATE City

SEND TO Same
STREET
SUBURB OR CITY STATE

HOW SOLD	DATE	SALES NUMBER	DEPT NO	IF C. O. D. COLLECT
Chg	9/18	51-A		

CONTENTS Merchandise.
POSTMASTER This package may be opened for postal inspection if necessary Return postage guaranteed

W. L. MANN	DATE	SALES NO	DEPT.
114- 3	9/18	51-A	

NO. ENCL.	HOW SOLD	AMT SOLD	AMT RECD.	DEPOSIT
	Chg	81.60		

BOUGHT BY W.H. Hayt CUSTOMER'S SIGNATURE W. H. Hayt

QUAN.	ARTICLES	AMOUNT	
1	Buffet, Mhg	65	00
1	Coffee Table, Mhg	16	60
		81	60

Entered 9/19 O.W.
Posted 9/19 O.W.

OFFICE RECORD

Illustration No. 4, Sales Ticket

sales, it is necessary to prepare a handwritten sales ticket or charge slip for every credit sale. Such sales tickets are usually prepared in duplicate or in triplicate. The original copy is for the bookkeeping department, while a carbon copy is given to the customer. Where more than one salesperson is employed, each is usually provided with his own pad of sales tickets. Each pad bears a different number that identifies the clerk. The individual sales tickets are also numbered consecutively. This facilititates sorting the tickets by clerks if it is desired to compute the amount of goods sold by each clerk. Reference to the sales ticket reproduced on page 52 will show the type of information and the manner in which it is usually recorded.

When merchandise is sold for cash, the transaction results in an increase in the asset cash with a corresponding increase in sales income; hence it should be recorded by debiting Cash and by crediting Sales. When merchandise is sold on credit, the transaction results in an increase in the asset accounts receivable with a corresponding increase in sales income; hence it should be recorded by debiting Accounts Receivable and by crediting Sales.

Accounts Receivable. In order that the proprietor may know the total amount due from charge customers at any time, it is advisable to keep a summary ledger account with Accounts Receivable. This is an asset account. The debit balance of the account at the beginning of the period represents the total amount due from customers. During the period, the account should be debited for the amount of any transactions involving increases and should be credited for the amount of any transactions involving decreases in the amount due from his customers. At the end of the period, the debit balance of the account again represents the total amount due from customers.

It is also necessary to keep some record of the transactions completed with each customer in order that information may be readily available at all times as to the amount due from each customer. The following methods of accounting for charge sales are widely used:

(*a*) ***The sales ticket method.*** Under this method it is customary to file the charge sales tickets systematically. All other vouchers or documents representing transactions with customers should be filed with the sales tickets. Special filing equipment facilitates the use of this method. In some cases a chronological record of the charge sales tickets is kept as a means of control.

(*b*) ***The ledger account method.*** Under this method it is customary to keep a chronological record of the charge sales tickets. An individual ledger account with each customer is also kept. Special equipment may be used in maintaining a permanent file of the charge sales tickets and other vouchers or documents supporting the records.

Under either of these methods of accounting for transactions with charge customers it is necessary that a sales ticket or charge slip be made for each sale on credit. In making a charge sales ticket the date, the name and address of the customer, the quantity, a description of the items sold, the unit prices, and the total amount of the sale should be recorded. In some cases the old balance is entered at the top of the ticket and the new balance is shown at the bottom. Under this plan it is only necessary to refer to the most recent charge sales ticket to ascertain the amount due from a particular customer.

Sales Journal. Transactions involving the sale of merchandise on credit can be recorded in an ordinary two-column general journal. In a mercantile enterprise, sales transactions occur frequently. In a business where the proprietor follows the practice of selling merchandise on credit, such transactions may be recorded in a special journal advantageously. One form of *sales journal* is illustrated below. The following transactions, representing sales on credit by P. A. Mosely, a retail merchant, during the month of May, are shown recorded in the illustration. All charge sales are payable by the tenth of the following month.

May 5. T. L. Britton, 1214 Walnut Street, City; Sale No. 61; $205.
5. W. A. Bain, 1609 Main Street, City; Sale No. 62; $1,175.
11. E. M. Hall, 932 Day Street, City; Sale No. 63; $425.50.
15. H. B. Boyd, 617 Davis Avenue, City; Sale No. 64; $1,262.75.
22. T. L. Britton; Sale No. 65; $725.
26. E. M. Hall; Sale No. 66; $1,165.20.

54 SALES JOURNAL FOR MONTH OF May 19–

Date of Entry		No. of Sale	To Whom Sold	Post. Ref.	Amount	
			Amount Forwarded			
May	5	61	T. L. Britton	✓	205	00
	5	62	W. A. Bain	✓	1 175	00
	11	63	E. M. Hall	✓	425	50
	15	64	H. B. Boyd	✓	1 262	75
	22	65	T. L. Britton	✓	725	00
	26	66	E. M. Hall	✓	1 165	20
	31	67	Accounts Receivable Dr.-Sales Cr.	10/30	4 958	45

Sales Journal

It will be noted that the following information regarding each charge sales ticket is recorded in the sales journal:

(a) Date on which the sale is recorded.
(b) Number of the sales ticket.
(c) To whom sold (the customer).
(d) Amount of the sale.

With this form of sales journal, each transaction can be recorded on one horizontal line. The sales ticket should provide all the information needed in recording the sale.

If an individual ledger account is not kept with each customer, the charge sales tickets should be filed immediately after they have been recorded in the sales journal. They are usually filed alphabetically under the name of the customer. There are numerous types of trays, cabinets, and files on the market that are designed to facilitate the filing of charge sales tickets by customers. Such devices are designed to save time, to promote accuracy, and to provide a safe means of keeping a record of the transactions with each charge customer.

When a customer makes a partial payment on his account, the amount of the payment should be noted on the most recent charge sales ticket and the new balance should be indicated. Sales tickets paid in full should be receipted and may either be given to the customer or may be transferred to another file for future reference. If a customer is given credit for merchandise returned or because of allowances, a notation of the amount of credit should be made on the most recent charge sales ticket and the new balance should be indicated. If a credit memorandum is issued to a customer it should be prepared in duplicate and the carbon copy should be attached to the sales ticket on which the amount is noted.

Posting from the Sales Journal. Under the sales ticket method of accounting for charge sales, individual posting from the sales journal is not required. When this plan is followed, it is customary to place a check mark in the Posting Reference column of the sales journal at the time of entering each sale.

At the end of the month the Amount column of the sales journal should be footed, the total recorded, and the ruling completed as illustrated. The total charge sales for the month should be posted as a debit to Accounts Receivable and as a credit to Sales. When posting this item, it is advisable to write "Total charge sales" in the Items column of the accounts with Accounts Receivable and Sales. The titles of both accounts and the posting references may be entered on one horizontal line of the sales journal as shown in the illustration.

Under this plan of accounting, the proprietor need only refer to the accounts receivable account to ascertain the total amount due from his customers at any time. The balance of the account may be proved by ascertaining the total of the unpaid balances of the sales tickets kept in the customers' file.

Schedule of Accounts Receivable. It is usually advisable at the end of each month to prepare a list of customers showing the name of each customer and the amount due from him. This is known as a *schedule of accounts receivable.* Such a schedule can be prepared easily by going through the customers' file and listing the names of the customers and the amount due from each. Should the total not be in agreement with the balance of the summary account with Accounts Receivable, it is an indication that an error has been made either in recording the transactions with customers in the summary account with Accounts Receivable or in handling the charge sales tickets. If the error is in the summary account, it will usually be revealed by the trial balance. If the general ledger accounts are in balance, it will indicate that the error has probably been made in handling the charge sales tickets.

If an individual ledger account is kept with each customer, all transactions representing either increases or decreases in the amount due from each customer should be posted individually to the proper account. The posting may be done by hand or posting machines may be used. If the posting is done by hand, it may be completed either direct from the charge sales tickets and other vouchers or documents representing the transactions, or it may be completed from the books of original entry. If the posting is done with posting machines, it will usually be completed direct from the charge sales tickets and other vouchers or documents.

General Journal. When a purchases journal, a sales journal, and a general journal are used as the only books of original entry, all purchases of merchandise on credit should be recorded in the purchases journal, all sales of merchandise on credit should be recorded in the sales journal, and all other transactions should be recorded in the general journal. All entries in the general journal should be posted individually to the proper accounts in the ledger. At the end of the month, the total credit purchases for the month should be posted in one amount to the debit of Purchases and to the credit of Accounts Payable. At the same time, the total charge sales for the month should be posted in one amount to the debit of Accounts Receivable and to the credit of Sales. Thus the use of a purchases journal and a sales journal saves considerable time in posting.

Application of Principles. To illustrate the effect on the merchandise accounts of transactions arising from the purchase and sale of merchandise, the following selected transactions are analyzed and entered in appropriate "T" accounts.

NARRATIVE OF TRANSACTIONS

May 1. P. A. Mosely invested $10,000 cash in a retail merchandising business

Analysis: This transaction established the amount of the proprietor's investment in the business. It should be recorded by debiting Cash and by crediting P. A. Mosely, Proprietor, for $10,000. While this transaction does not affect the merchandise accounts, it is included in order to provide the cash needed in making cash purchases.

May 4. Purchased merchandise from D. A. Crowe, 824 Fourth St., City, for cash, $65.

Analysis: This transaction resulted in acquiring merchandise for sale and involved a decrease in the asset cash. It should be recorded by debiting Purchases and by crediting Cash for $65.

May 6. Cash sales per cash register tape, $257.35.

Analysis: This transaction had the effect of increasing the asset cash and resulted in income from sales. It should be recorded by debiting Cash and by crediting Sales for $257.35.

May 12. Paid Dobson Bros. $778.92 on account.

Analysis: This transaction had no effect on the merchandise accounts. It resulted in a decrease in the asset cash and a corresponding decrease in accounts payable. It should be recorded by debiting Accounts Payable and by crediting Cash for $778.92.

May 15. Received $205 from T. L. Britton on account.

Analysis: This transaction had no effect on the merchandise accounts. It resulted in an increase in the asset cash and a corresponding decrease in accounts receivable. It should be recorded by debiting Cash and by crediting Accounts Receivable for $205.

May 18. Received credit for merchandise returned to A. W. Shaw Co., $14.95.

Analysis: This transaction resulted in an increase in purchases returns with a corresponding decrease in accounts payable. It should be recorded by debiting Accounts Payable and by crediting Purchases Returns and Allowances for $14.95.

May 20. Allowed credit for merchandise returned by E. M. Hall, $12.

Analysis: This transaction resulted in a decrease in accounts receivable with a corresponding increase in sales returns. It should be recorded by debiting Sales Returns and Allowances and by crediting Accounts Receivable for $12.

May 20. Cash sales per cash register tape, $204.20.

May 22. Paid the Lawton Drayage Co. $27.45 for freight and drayage on merchandise purchased.

Analysis: This transaction resulted in an increase in the cost of merchandise purchased and a decrease in cash. It should be recorded by debiting Purchases and by crediting Cash for $27.45.

(Continued on page 59)

ACCOUNTS OF P. A. MOSELY

Cash

May 1	10,000 00	May 4	65.00
6	257.35	12	778.92
15	205.00	22	27.45
20	204.20		*871.37*
9,795.18	*10,666.55*		

Accounts Receivable

May 31	4,958.45	May 15	205.00
4,741.45		20	12.00
			217.00

Accounts Payable

May 12	778.92	May 31	3,767.62
18	14.95	*2,955.55*	
24	18.20		
	812.07		

P. A. Mosely, Proprietor

		May 1	10,000.00

Sales

		May 6	257.35
		20	204.20
		31	4,958.45
			5,420.00

Sales Returns and Allowances

May 20	12.00		

Purchases

May 4	65.00		
22	27.45		
31	3,767.62		
	3,860.07		

Purchases Returns and Allowances

		May 18	14.95
		24	18.20
			33.15

The transactions completed by P. A. Mosely are shown recorded in the "T" accounts at the left. The accounts have been footed and the balances recorded on the proper side in small pencil figures.

The equality of the account balances may be proved by taking a trial balance. The balance of the accounts receivable summary account may be proved by preparing a schedule of accounts receivable and ascertaining the total amount due from customers. The charge sales tickets in the customers' file are the source of the information needed in preparing this schedule.

The balance of the accounts payable summary account may be proved by preparing a schedule of accounts payable and ascertaining the total amount due to creditors. The unpaid invoice file is the source of the information needed in preparing this schedule.

TRIAL BALANCE OF P. A. MOSELY

Cash	$ 9,795.18	
Accounts Rec.	4,741.45	
Accounts Pay.		$ 2,955.55
P. A. Mosely, Prop.		10,000.00
Sales		5,420.00
Sales R. & A.	12.00	
Purchases	3,860.07	
Purchases R. & A.		33.15
	$18,408.70	$18,408.70

SCHEDULE OF ACCOUNTS RECEIVABLE

W. A. Bain	$1,175.00
H. B. Boyd	1,262.75
T. L. Britton	725.00
E. M. Hall	1,578.70
Total	$4,741.45

SCHEDULE OF ACCOUNTS PAYABLE

Dobson Bros.	$1,398.60
Gray Mfg. Co.	1,185.40
A. W. Shaw Co.	371.55
Total	$2,955.55

May 24. Received credit from Gray Mfg. Co. for inferior merchandise, $18.20.

Analysis: This transaction resulted in an increase in purchases allowances with a corresponding decrease in accounts payable. It should be recorded by debiting Accounts Payable and by crediting Purchases Returns and Allowances for $18.20.

May 31. Total merchandise purchased on credit during the month, per purchases journal, $3,767.62.

Analysis: Mr. Mosely's purchases journal for May is reproduced on page 49. The use of a purchases journal for recording invoices representing merchandise purchased on credit makes it possible to post the total credit purchases for the month in one amount by debiting Purchases and by crediting Accounts Payable for $3,767.62.

May 31. Total merchandise sold on credit during the month, per sales journal, $4,958.45.

Analysis: Mr. Mosely's sales journal for May is reproduced on page 54. The use of a sales journal for recording charge sales tickets makes it possible to post the total charge sales for the month in one amount by debiting Accounts Receivable and by crediting Sales for $4,958.45.

PRACTICE ASSIGNMENT No. 4. Refer to the workbook and complete Report No. 4. To be able to complete this practice assignment correctly, the principles developed in the preceding discussion must be understood. Review the text assignment if necessary. After completing the report, continue with the following study assignment until the next report is required.

V GROSS PROFIT ON SALES

The gross profit on sales is determined by deducting the cost of the goods sold from the net sales. When separate merchandise accounts are kept for purchases, purchases returns and allowances, sales, sales returns and allowances, and merchandise inventory, it is a relatively simple matter to determine the gross profit on sales for any period. The use of inventories at the beginning and the end of each year is required by income tax regulations in every case in which the purchase or the sale of merchandise is an income-producing factor. When an inventory is taken at the end of each year, the cost of the merchandise in stock at the end of each year and at the beginning of the following year will be known.

Taking an Inventory. In taking an inventory, it is necessary to count the number of units of each article in stock and to determine the price at which each unit is to be valued. The amount of each article is then calculated, and the total value of all goods in stock is ascertained. There are different bases of valuing inventories; however, the only basis that will be considered at this point is the cost basis, and it will be assumed that the cost of each item is the unit price paid on the most recent purchase. This is known as the *first-in, first-out* (Fifo) method of inventorying merchandise. It is based on the theory that the goods first purchased are the goods first sold and that the goods on hand at the close of the period are the goods most recently purchased. The merchandise inventory taken by P. A. Mosely, a retail merchant, at the close of the year follows:

P. A. MOSELY'S MERCHANDISE INVENTORY

QUANTITY	ITEM	UNIT PRICE	AMOUNT
5	Dining room suite	$ 94.90	$ 474.50
4	Living room suite	127.50	510.00
6	Bedroom suite	87.10	522.60
4	Dinette	66.85	267.40
7	Chair — reclining	40.15	281.05
20	Chair — rocker	31.20	624.00
7	Chair — occasional	27.25	190.75
4	Studio couch	49.15	196.60
10	Table	18.25	182.50
13	End table	6.30	81.90
11	Coffee table	18.90	207.90
7	Book case	26.90	188.30
6	Desk	22.75	136.50
18	Wall rack	2.20	39.60
18	Magazine rack	3.90	70.20
20	Table lamp	9.60	192.00
13	Bed lamp	1.85	24.05
25	Floor lamp	18.70	467.50
20	Boudoir lamp	2.70	54.00
13	Cedar chest	24.90	323.70
23	Hassock	6.45	148.35
			$5,183.40

Cost of Sales. The cost of merchandise sold is usually referred to as the *cost of sales.* In computing the cost of sales for any accounting period, it is necessary to take into consideration (a) the amount of the inventory, if any, at the beginning of the period; (b) the cost of goods purchased during the period; (c) the total amount of any returns and allowances during the period; and (d) the amount of the inventory, if any, at the end of the period.

In the illustrations that follow, varying factors are introduced to show the methods used in computing Mr. Mosely's cost of sales:

(a)

Merchandise inventory, beginning of period	None
Purchases	$7,428.50
Purchases returns and allowances	75.00
Merchandise inventory, end of period	None

COMPUTATION OF COST OF SALES

Purchases	$7,428.50
Less purchases returns and allowances	75.00
Cost of sales	$7,353.50

(b)

Merchandise inventory, beginning of period	None
Purchases	$7,428.50
Purchases returns and allowances	75.00
Merchandise inventory, end of period	5,183.40

COMPUTATION OF COST OF SALES

Purchases	$7,428.50
Less purchases returns and allowances	75.00
Net purchases	$7,353.50
Less merchandise inventory, end of period	5,183.40
Cost of sales	$2,170.10

(c)

Merchandise inventory, beginning of period	$5,733.40
Purchases	7,428.50
Purchases returns and allowances	75.00
Merchandise inventory, end of period	5,183.40

COMPUTATION OF COST OF SALES

Merchandise inventory, beginning of period	$5,733.40
Purchases	7,428.50
Total	$13,161.90
Less purchases returns and allowances	75.00
Cost of merchandise available for sale	$13,086.90
Less merchandise inventory, end of period	5,183.40
Cost of sales	$7,903.50

Gross Profit on Sales. After ascertaining the cost of sales, the gross profit on sales, sometimes referred to as the *margin on sales,* may be ascertained by deducting the cost of sales from the net sales for the period.

The accounts with sales and sales returns and allowances should provide the information needed in computing the net sales. The balance of the sales account represents the total selling price of all goods sold during the period, while the balance of the sales returns and allowances account represents the selling price of all merchandise returned by customers plus allowances made to customers that decreased the selling price of the merchandise sold. Assuming that Mr. Mosely's sales for the period represented by the credit balance of his sales account amounted to $12,044.50 and that the debit balance of his sales returns and allowances account amounted to $122.50, his gross profit on sales for the period under the three illustrations may be computed as follows:

	(a)	(b)	(c)
Sales	$12,044.50	$12,044.50	$12,044.50
Less sales returns and allowances	122.50	122.50	122.50
Net sales	$11,922.00	$11,922.00	$11,922.00
Less cost of sales	7,353.50	2,170.10	7,903.50
Gross profit on sales	$ 4,568.50	$ 9,751.90	$ 4,018.50

To illustrate further, it will be assumed that the following information with respect to operations for the month of January was obtained from the accounts of J. A. Lamb, a radio and television dealer:

(a)	Sales	$3,164
(b)	Sales returns and allowances	132
(c)	Inventory of merchandise on hand, beginning of month	1,200
(d)	Purchases	2,240
(e)	Purchases returns and allowances	115
(f)	Inventory of merchandise on hand, end of month	1,375

STATEMENT OF GROSS PROFIT ON SALES FOR JANUARY

Sales			3,164	00
Less Sales Returns and Allowances			132	00
Net Sales			3,032	00
Less Cost of Sales:				
Merchandise Inventory, beginning of month	1,200	00		
Purchases	2,240	00		
Total	3,440	00		
Less Purchases Returns and Allowances	115	00		
Cost of Merchandise Available for Sale	3,325	00		
Less Merchandise Inventory, end of month	1,375	00	1,950	00
Gross Profit on Sales			1,082	00

PRACTICE ASSIGNMENT No. 5. Refer to the workbook and complete Report No. 5. To be able to complete this practice assignment correctly, the principles developed in the preceding discussion must be understood. Review the text assignment if necessary. After completing the report, continue with the following study assignment until the next report is required.

VI ACCOUNTING PROCEDURE

The accounting procedure in recording the transactions of a mercantile enterprise is, in general, the same as that involved in recording the transactions of any other enterprise. In a small mercantile enterprise where the number of transactions is not large and all the bookkeeping may be done by one person, a standard two-column journal may be used as the only book of original entry. However, if desired, a purchases journal and a sales journal may be used along with the general journal. The purchases journal may be used for keeping a chronological record of purchases of merchandise on credit and the sales journal may be used for keeping a chronological record of sales of merchandise on credit. All of the accounts may be kept in one general ledger which may be either a bound book or a loose-leaf book. The posting may be completed daily or periodically.

A trial balance should be taken at the end of each month as a means of proving the equality of the account balances. The balance of the summary account with Accounts Receivable should be proved periodically, or at least at the end of each month. This may be done by ascertaining the total of the unpaid sales tickets or charge slips that are kept in a customers' file. Likewise, the balance of the summary account with Accounts Payable should be proved periodically, or at least at the end of each month. This may be done by ascertaining the total of the unpaid invoices that are kept in an unpaid invoice file.

This procedure will be illustrated by (a) recording a narrative of transactions for one month in a purchases journal, a sales journal, and a general journal, (b) by posting to the ledger accounts, (c) by taking a trial balance to prove the equality of the account balances at the end of the month, (d) by preparing a schedule of accounts receivable to prove the balance of the summary account with Accounts Receivable, and (e) by preparing a schedule of accounts payable to prove the balance of the summary account with Accounts Payable.

W. A. Goodrich is the owner and operator of a small retail business. He uses a purchases journal, a sales journal, and a standard two-column general journal as books of original entry. All of his accounts are kept in a bound general ledger. Individual ledger accounts with customers and creditors are not kept; instead, the purchase invoices and the charge sales tickets are filed in the manner previously described in this unit. All credit sales are payable by the tenth of the following month unless otherwise agreed. His chart of accounts appears at the top of the following page.

CHART OF ACCOUNTS

W. A. GOODRICH

Assets
- Cash
- Accounts Receivable
- Merchandise Inventory
- Store Equipment

Liabilities
- Accounts Payable

Proprietorship
- W. A. Goodrich, Proprietor
- W. A. Goodrich, Drawing

Income
- Sales
- Sales Returns and Allowances

Cost
- Purchases
- Purchases Returns and Allowances

Expenses
- Rent Expense
- Advertising Expense
- Telephone Expense
- Salaries

NARRATIVE OF TRANSACTIONS

W. A. Goodrich, Proprietor

Wednesday, March 1

W. A. Goodrich started in business with a cash investment of $2,000.

Rented a storeroom located at 934 High Street and paid one month's rent in advance, $95.

Thursday, March 2

Purchased merchandise for cash from Brown Bros., 820 Park St., City, $79.30.

Friday, March 3

Received Invoice No. 1 dated March 1 from King and King, 16 York St., City, for merchandise purchased, $136.95. Terms, 30 days net.

Saturday, March 4

Sold merchandise on credit to A. Y. Jordan, 115 Main St., City, $16.25. Sale No. 1–1.

Purchased store equipment from Logan Bros., 410 Vine St., City, $185. Terms, 30 days net.

Since this transaction involves a purchase of store equipment, it was recorded in the general journal; the purchases journal is used only for recording transactions arising from the purchase of merchandise on credit.

Sundry cash sales per cash register tape, $32.

Mr. Goodrich records the sundry cash sales for each week on Saturday, using the cash register tape as the source of the amount.

Monday, March 6

Purchased merchandise for cash from Brown Bros., $194.

Sold merchandise on credit to Peoples Hotel, 165 Willis St., City, $59.35. Sale No. 1–2.

Tuesday, March 7

Gave the Peoples Hotel credit for merchandise returned, $9.10.

This transaction had the effect of increasing sales returns and allowances and decreasing the amount due from the Peoples Hotel.

Thursday, March 9

Sold merchandise on credit to A. Y. Jordan, 115 Main St., City, $56.25. Sale No. 2–1.

Received Invoice No. 2 dated March 8 from King and King, 16 York St., City, for merchandise purchased, $230. Terms, 30 days net.

Friday, March 10

Sold merchandise on credit to James O. Wills, 416 Broad St., City, $44.30. Sale No. 2–2.

Saturday, March 11

Sundry cash sales per cash register tape, $54.

Wednesday, March 15

Paid sales clerk's semimonthly wages in cash, $57.50.

Received Invoice No. 3 dated March 13 from Lake View Creamery, Dayton, for merchandise purchased, $30. Terms, 30 days net.

Thursday, March 16

Received a check for $16.25 from A. Y. Jordan in payment of merchandise sold him on March 4.

Paid King and King $136.95 in settlement of their invoice of March 1.

Friday, March 17

Sold merchandise on credit to J. C. Wells, 765 E. Ninth St., City, $26.05. Sale No. 3–2.

Saturday, March 18

Received credit for $12.60 from King and King for merchandise returned by agreement.

This transaction had the effect of increasing purchases returns and allowances and decreasing the amount due King and King.

Sundry cash sales per cash register tape, $84.50.

Monday, March 20

Paid cash for newspaper advertising, $15.

Sold merchandise on credit to Peoples Hotel, 165 Willis St., City, $82.05. Sale No. 3–1.

Wednesday, March 22

Received Invoice No. 4 dated March 20 from Lake View Creamery for merchandise purchased, $37.50. Terms, 30 days net.

Thursday, March 23

Sold merchandise on credit to Peoples Hotel, 165 Willis St., City, $80.25. Sale No. 4–1.

Friday, March 24

Paid freight and drayage on merchandise purchased, $27.50.

Saturday, March 25

Received remittance for $50.25 from Peoples Hotel in payment of the balance due on merchandise sold on March 6.

Sundry cash sales per cash register tape, $78.40.

Monday, March 27

Purchased merchandise for cash from Brown Bros., $199.10.

Sold merchandise on credit to James O. Wills, 416 Broad St., City, $137.56. Sale No. 4–2.

Wednesday, March 29

Received remittance for $44.30 from James O. Wills in payment of merchandise sold him on March 10.

Sold merchandise on credit to J. C. Wells, 765 E. Ninth St., City, $151.40. Sale No. 5–2.

Thursday, March 30

Received remittance for $26.05 from J. C. Wells in payment of merchandise sold him on March 17.

Paid Logan Bros. $85 on account.

Received credit for $4 from Lake View Creamery for inferior merchandise.

Friday, March 31

Sundry cash sales per cash register tape, $57.60.

Inasmuch as this is the last day of the month, the amount of the cash sales for the week to date was ascertained from the cash register tape and recorded.

Paid telephone bill for March service, $8.

Paid sales clerk's semimonthly wages in cash, $57.50.

W. A. Goodrich withdrew $80 in cash for personal use.

PURCHASES JOURNAL FOR MONTH OF *March* 19–67

DATE OF ENTRY		DATE OF INVOICE		NO. OF INVOICE	FROM WHOM PURCHASED	POST. REF.	AMOUNT	DATE PAID	
					AMOUNT FORWARDED				
Mar	3	Mar	1	1	King & King	✓	136 95	Mar	16
	9		8	2	King & King	✓	230 00		
	15		13	3	Lake View Creamery	✓	30 00		
	22		20	4	Lake View Creamery	✓	37 50		
	31				Purchases Dr.–Accounts Payable Cr.	9/14	434 45		

W. A. Goodrich's Purchases Journal

SALES JOURNAL FOR MONTH OF *March* 19–67

DATE OF ENTRY		NO. OF SALE	TO WHOM SOLD	POST. REF.	AMOUNT
			AMOUNT FORWARDED		
Mar	4	1-1	A. Y. Jordan	✓	16 25
	6	1-2	Peoples Hotel	✓	59 35
	9	2-1	A. Y. Jordan	✓	56 25
	10	2-2	James O. Wills	✓	44 30
	17	3-2	J. C. Wells	✓	26 05
	20	3-1	Peoples Hotel	✓	82 05
	23	4-1	Peoples Hotel	✓	80 25
	27	4-2	James O. Wills	✓	137 56
	29	5-2	J. C. Wells	✓	151 40
	31		Accounts Receivable Dr.–Sales Cr.	2/7	653 46

W. A. Goodrich's Sales Journal

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GENERAL JOURNAL

Date		Description	Post. Ref.	Debits	Credits
Mar.	1	Cash	1	2000 00	
		W. A. Goodrich, Proprietor	5		2000 00
		Invested in business.			
	1	Rent Expense	11	95 00	
		Cash	1		95 00
		Storeroom rent for March.			
	2	Purchases	9	79 30	
		Cash	1		79 30
		Brown Bros.			
	4	Store Equipment	3	185 00	
		Accounts Payable	4		185 00
		Logan Bros.			
	4	Cash	1	32 00	
		Sales	7		32 00
		Sundry cash sales.			
	6	Purchases	9	194 00	
		Cash	1		194 00
		Brown Bros.			
	7	Sales Ret. & Al.	8	9 10	
		Accounts Receivable	2		9 10
		Mdse. retd.—Peoples Hotel.			
	11	Cash	1	54 00	
		Sales	7		54 00
		Sundry cash sales.			
	15	Salaries	14	57 50	
		Cash	1		57 50
		Sales clerk.			
	16	Cash	1	16 25	
		Accounts Receivable	2		16 25
		A. Y. Jordan; Inv. of Mar. 4.			
	16	Accounts Payable	4	136 95	
		Cash	1		136 95
		King & King. Inv. of Mar. 1.			
	18	Accounts Payable	4	12 60	
		Purchases Ret. & Al.	10		12 60
		Mdse. retd.—King & King.			
	18	Cash	1	84 50	
		Sales	7		84 50
		Sundry cash sales.			
				2956 20	2956 20

W. A. Goodrich's General Journal

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Date		Description	Post. Ref.	Debits	Credits
19—					
Mar	20	Advertising Expense	12	15 00	
		Cash	1		15 00
		Newspaper advertising.			
	24	Purchases	9	27 50	
		Cash	1		27 50
		Freight and drayage.			
	25	Cash	1	50 25	
		Accounts Receivable	2		50 25
		Peoples Hotel, Inv. of Mar. 6.			
	25	Cash	1	78 40	
		Sales	7		78 40
		Sundry cash sales.			
	27	Purchases	9	199 10	
		Cash	1		199 10
		Brown Bros.			
	29	Cash	1	44 30	
		Accounts Receivable	2		44 30
		James O. Wills, Inv. of Mar. 10.			
	30	Cash	1	26 05	
		Accounts Receivable	2		26 05
		J. C. Wells, Inv. of Mar. 17.			
	30	Accounts Payable	4	85 00	
		Cash	1		85 00
		Logan Bros., on account.			
	30	Accounts Payable	4	4 00	
		Purchases Ret. & Al.	10		4 00
		Lake View Creamery-allowance			
	31	Cash	1	57 60	
		Sales	7		57 60
		Sundry cash sales.			
	31	Telephone Expense	13	8 00	
		Cash	1		8 00
		March telephone bill.			
	31	Salaries	14	57 50	
		Cash	1		57 50
		Sales clerk.			
	31	W. A. Goodrich, Drawing	6	80 00	
		Cash	1		80 00
		Personal use.			
				7 3 2 7 0	7 3 2 7 0
				732 70	732 70

W. A. Goodrich's General Journal (Concluded)

GENERAL LEDGER

ACCOUNT *Cash* Page 1

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19–						19–					
Mar.	1		J68		2,000.00	Mar.	1		J68		95.00
	4		J68		32.00		2		J68		79.30
	11		J68		54.00		6		J68		194.00
	16		J68		16.25		15		J68		57.50
	18		J68		84.50		16		J68		136.95
	25		J69		50.25		20		J69		15.00
	25		J69		78.40		24		J69		27.50
	29		J69		44.30		27		J69		199.10
	30		J69		26.05		30		J69		85.00
	31		J69		57.60		31		J69		8.00
							31		J69		57.50
							31		J69		80.00

ACCOUNT *Accounts Receivable* Page 2

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19–						19–					
Mar.	31	Total charge sales	S67		653.46	Mar.	7		J68		9.10
							16		J68		16.25
							25		J69		50.25
							29		J69		44.30
							30		J69		26.05

ACCOUNT *Store Equipment* Page 3

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19–											
Mar.	4		J68		185.00						

W. A. Goodrich's General Ledger

ACCOUNT *Accounts Payable* — Page 4

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19—						19—					
Mar.	16		J68		136 95	Mar.	4		J68		185 00
	18		J68		12 60		31	Total Cr. purchases	P67		434 45
	30		J69		85 00						
	30		J69		4 00						

ACCOUNT *W. A. Goodrich, Proprietor* — Page 5

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19—					
						Mar.	1		J68		2000 00

ACCOUNT *W. A. Goodrich, Drawing* — Page 6

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19—											
Mar.	31		J69		80 00						

ACCOUNT *Sales* — Page 7

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19—					
						Mar.	4		J68		32 00
							11		J68		54 00
							18		J68		84 50
							25		J69		78 40
							31		J69		57 60
							31	Total charge sales	S67		653 46

ACCOUNT *Sales Returns and Allowances* — Page 8

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19—											
Mar.	7		J68		9 10						

W. A. Goodrich's General Ledger (Continued)

ACCOUNT *Purchases* Page 9

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar	2		J68		79 30						
	6		J68		194 00						
	24		J69		27 50						
	27		J69		199 10						
	31	Total Cr. purchases	P 67		434 45						

ACCOUNT *Purchases Returns and Allowances* Page 10

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Mar	18		J68		12 60
							30		J69		4 00

ACCOUNT *Rent Expense* Page 11

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar	1		J68		95 00						

ACCOUNT *Advertising Expense* Page 12

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar	20		J69		15 00						

ACCOUNT *Telephone Expense* Page 13

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar	31		J69		8 00						

ACCOUNT *Salaries* Page 14

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar	15		J68		57 50						
	31		J69		57 50						

W. A. Goodrich's General Ledger (Concluded)

W. A. Goodrich
Trial Balance, March 31, 19–

Accounts	Page	Dr. Balances	Cr. Balances
Cash	1	1408 50	
Accounts Receivable	2	507 51	
Store Equipment	3	185 00	
Accounts Payable	4		380 90
W. A. Goodrich, Proprietor	5		2000 00
W. A. Goodrich, Drawing	6	80 00	
Sales	7		959 96
Sales Returns and Allowances	8	9 10	
Purchases	9	934 35	
Purchases Returns and Allowances	10		16 60
Rent Expense	11	95 00	
Advertising Expense	12	15 00	
Telephone Expense	13	8 00	
Salaries	14	115 00	
		3357 46	3357 46
Schedule of Accounts Receivable			
A. Y. Jordan	✓	56 25	
Peoples Hotel	✓	162 30	
J. C. Wells	✓	151 40	
James O. Wills	✓	137 56	
Total Accounts Receivable		507 51	
Schedule of Accounts Payable			
King & King	✓		217 40
Lake View Creamery	✓		63 50
Logan Bros.	✓		100 00
Total Accounts Payable			380 90

W. A. Goodrich's Trial Balance and Schedules

Journalizing. The transactions completed by Mr. Goodrich during the month of March were recorded in the purchases journal reproduced on page 67, the sales journal reproduced on page 67, and the general journal reproduced on pages 68 and 69.

Posting. Mr. Goodrich's ledger is reproduced on pages 70 to 72. The posting was completed from the books of original entry in the following order: first, the general journal; second, the purchases journal; and, third, the sales journal. Each entry in the general journal was posted individually to the proper accounts. The only posting that was done from the purchases and sales journals was the summary posting required at the end of the month. The total of the credit purchases was posted in one amount as a debit to Purchases and a credit to Accounts Payable. The total of the charge sales was posted in one amount as a debit to Accounts Receivable and a credit to Sales. As the posting was completed, the proper cross references were indicated in the Posting Reference columns of the books of original entry and in the Folio columns of the ledger.

When more than one book of original entry is used, it is advisable to identify each book by means of an initial preceding the page number. The following code was used in conjunction with the page number to indicate the source of each entry in the ledger:

J = General journal
P = Purchases journal
S = Sales journal

Trial Balance. After the posting was completed, the accounts in the general ledger were footed and the balances were entered in the Items column on the proper side. The trial balance reproduced on page 73 was taken to prove the equality of the account balances. The balance of the accounts receivable summary account was proved by preparing a schedule of accounts receivable. The information needed in preparing this schedule was obtained from the sales tickets in the customers' file. The balance of the accounts payable summary account was proved by preparing a schedule of accounts payable. The information needed in preparing this schedule was obtained from the invoices in the unpaid invoice file. These schedules are reproduced following the trial balance.

Gross Profit on Sales. If Mr. Goodrich wishes to compute the gross profit on sales for the month, it will be necessary first to take an inventory of merchandise in stock at the end of the month. Assuming that an inventory was taken and that it showed that he had merchandise on hand March 31 amounting to $290.65, the gross profit on sales for March may be computed in the following manner:

STATEMENT OF GROSS PROFIT ON SALES FOR MARCH

Sales			959	96
Less Sales Returns and Allowances			9	10
Net Sales			950	86
Less Cost of Sales:				
Purchases	934	35		
Less Purchases Returns and Allowances	16	60		
Net Purchases	917	75		
Less Merchandise Inventory, end of month	290	65	627	10
Gross Profit on Sales			323	76

Finding Errors. There are certain types of errors that a trial balance may not reveal, such as the following:

(a) Failure to record a transaction in the books of original entry.

(b) Failure to post both debit and credit items of equal amount recorded in a book of original entry.

(c) Posting an item to the wrong account.

Such errors may be detected by checking to make sure (a) that all transactions have been recorded in the books of original entry, and (b) that all amounts recorded in the books of original entry have been correctly posted to the proper accounts in the ledger.

When the debit and the credit footings of a trial balance are unequal, the trial balance is out of balance. The trial balance can be brought into balance by checking or auditing the accounts and records until the error or errors are found and by making the necessary corrections. There is no standard procedure to be followed in making this check or audit, but it is advisable to follow a definite, logical plan or order of procedure. The following is a suggested plan:

(1) Prove the listing of the accounts in the trial balance by checking the account titles and the amounts with the ledger, making sure that the account balances are correctly listed in amount and position.

(2) Prove the account footings and balances by adding the debit and the credit items and ascertaining the difference between the footings of each account in the ledger.

(3) Prove the posting from the books of original entry to the accounts, checking each item both in the ledger and in the book of original entry.

(4) Prove the equality of the debit and the credit items recorded in each of the books of original entry.

In most cases errors that affect a trial balance will be revealed before the foregoing suggested checking procedure is completed. It should seldom be necessary to carry out the entire four-point program of checking to find errors in a trial balance.

Correcting Errors. When errors are found, corrections should be made. Errors may be made in recording transactions, in footing the columns in books of original entry, in posting, in footing the accounts in the ledger, in subtracting to ascertain the account balances, in listing the account balances in the trial balance, or in footing the trial balance. There are two approved methods of correcting such errors:

(a) By drawing a line through the incorrect item and inserting the correct item.

(b) By drafting a journal entry that will effect the necessary correction and posting the entry to the proper accounts.

An error in footing the columns of the books of original entry, in posting, in footing the accounts in the ledger, in determining the account balances, in listing the accounts in the trial balance, or in footing the trial balance may be corrected by crossing out the incorrect sum and recording the correct amount just above the erroneous amount or wherever it should be recorded. This is the usual plan followed by bookkeepers.

An error in recording a transaction in the books of original entry should preferably be corrected by means of a journal entry. For example, if it is found that in recording a transaction in the general journal, Rent Expense instead of Salaries had been debited erroneously for $75 and that the entry was already posted, a correcting entry may be made in the general journal debiting Salaries and crediting Rent Expense for $75.

When this journal entry is posted to the proper accounts in the ledger, a notation should be made in the Items column of each account to indicate that the entry is a correcting entry. When the journal entry method of correcting errors is used, it is not necessary to cross out the incorrect entries made originally, because the posting of the correcting entry from the journal accomplishes the desired result. In other words, the posting of the correcting journal entry eliminates the effect of the original error.

***PRACTICE ASSIGNMENT No. 6.** Refer to the workbook and complete Report No. 6. This practice assignment provides a test of your ability to apply the principles developed in Units One and Two of this textbook. The textbook and the workbook go hand in hand, each serving a definite purpose in the learning process. Inability to solve correctly any problem included in the report indicates that you have failed to master the principles developed in the textbook. After completing the report, you may proceed with the textbook discussion in Unit Three until the next report is required.*

Unit Three

ACCOUNTING FOR CASH

VII THE CASHBOOK

In the preceding units the fundamental principles of double-entry bookkeeping were introduced and applied to transactions arising from both mercantile and nonmercantile enterprises. A purchases journal, a sales journal, and a general journal were introduced as books of original entry. The procedure in journalizing, posting, and taking a trial balance was illustrated. Another step in developing the theory of accounts is to introduce additional records and accounts that may be used advantageously in recording transactions. This unit is devoted to a discussion of the principles involved in accounting for cash receipts and disbursements; and to the introduction of the cashbook and of the combined cash-journal.

The Cash Account. Transactions that result in increases in cash are recorded as debits to the cash account; transactions that result in decreases in cash are recorded as credits to the cash account. Normally the cash account will have a debit balance. However, when all of the cash has been paid out, the account will be in balance. A debit balance in the cash account represents either money on hand or in the bank, or both.

Cash Receipts. An accurate record of cash and cash items received should be kept. Cash includes coins and currency. Cash items include checks, drafts, and money orders.

When the amount of cash and the number of cash items received are sufficient to warrant it, a system may be used whereby all such receipts are listed by one individual, who may be the proprietor, a secretary, the cashier, the treasurer, or some other designated employee. Such a list is usually prepared daily in duplicate. One copy goes to the bookkeeper for recording purposes. The other copy is kept with the receipts until the deposit ticket has been prepared and checked with the actual receipts. In preparing a list of cash receipts, the information that is needed to identify each item should be recorded. The list may be either penwritten or typewritten.

The following table shows how a list of cash receipts may be prepared:

Date	From Whom Received	Nature of Remittance	Amount
19--			
Jan. 2	J. A. Jones	Check	$ 14.20
	Nesmith Bros.	Postal Money Order	24.50
	Orson & Johnson	Currency	20.00
	Hiram Bolsinger	Express Money Order	40.00
	Francis Lyon	Bank Draft	28.75
	Mrs. Frank C. Condon	Cashier's Check	19.25
Total Cash Receipts			$146.70

When numerous cash sales are involved, the amounts received are usually recorded in a cash register. The cash register tape provides a list of cash receipts for accounting purposes. If a cash register is not used, some form of receipt in duplicate should be used for each cash transaction. The customer should be given a copy and another copy should be retained for accounting purposes. Under such a plan the bookkeeper may not actually handle any cash; instead he records cash receipts from lists prepared by other persons. This system is sometimes referred to as a method of internal check. It is generally advocated by public accountants as a desirable practice.

Cash Disbursements. Disbursements may be made in cash or by bank check. When disbursement is made in cash, a receipt or a receipted voucher should be obtained as evidence of the payment. When disbursement is made by bank check, it is not necessary to obtain a receipt since the canceled check that is returned by the bank on which it was drawn serves as a receipt.

Recording Cash Receipts and Disbursements. In the preceding units, transactions involving the receipt or the disbursement of cash were recorded in the general journal along with other transactions. In many business enterprises, transactions involving the receipt or the disbursement of cash are more numerous than other types of transactions. Because of the frequency of such transactions and the desirability of maintaining a continuous check on cash in order to prove the cash balance at frequent intervals, it may be considered advisable to keep a separate record of cash receipts and cash disbursements.

There are many types of cash records used by individuals, business firms, organizations, and institutions in recording transactions involving the receipt and the payment of cash. When a separate record is kept of cash receipts, it is usually referred to as a *cash receipts journal.* When a separate record is kept of cash payments or disbursements, it is usually referred to as a *cash payments journal* or a *cash disbursements journal.* When cash receipts and cash payments are both recorded in the same book of account, the book is usually referred to as a *cashbook.*

The Cashbook. Cash receipts and cash payments may be recorded on opposite pages of a two-column cashbook. Entering receipts in such a cashbook involves recording the following information:

(a) Date on which the cash was received.
(b) Title of the account to be credited.
(c) A description of the transaction.
(d) Amount of cash received.

Entries on the left-hand page of the cashbook represent receipts; hence, merely by footing the amount column and thus ascertaining the total receipts, the aggregate increase in cash for a given period may be determined.

Entering payments in such a cashbook involves recording the following information:

(a) Date on which the cash was paid.
(b) Title of the account to be debited.
(c) A description of the transaction.
(d) Amount of cash paid.

Entries on the right-hand page of the cashbook represent payments; hence, merely by footing the amount column and thus ascertaining the total payments, the aggregate decrease in cash for a given period may be determined.

The Cashbook Illustrated. The cashbook reproduced on pages 80 and 81 consists of two pages of a cashbook in which the receipts and the payments of M. B. Roberts for the month of December are recorded. The receipts are recorded on the left-hand page and the payments on the right-hand page. Mr. Roberts is a consulting engineer engaged in professional practice on his own account. Since his income is derived principally from compensation for personal services, he follows the practice of not recording income until it is received in cash and of not recording expenses until they are paid in cash. A narrative of the cash transactions completed by Mr. Roberts during the month of December precedes the illustration.

NARRATIVE OF TRANSACTIONS

Dec. 1. (Friday) Cash balance, $2,929.50.
1. Paid December rent in advance, $100.
2. Received $120 from Thompson and Whitehead in payment of engineering fees.
4. Paid telephone bill, $6.25.
9. Paid dues in National Association of Consulting Engineers, $15.
12. Gave the Community Chest $15.
15. Paid The Williamson Co. $90 on account.
16. Paid secretary's salary for first half of month, $85.
18. Received $65 from The Lacey Manufacturing Co. in payment of engineering fees.
20. Received $250 from Johnson Bros. in payment of engineering fees.
23. Paid $3 for subscription to a professional magazine.
27. Paid Robbins Furniture Co. $25 on account.
28. Received $200 from The Brown Trucking Co. for engineering fees.
29. Paid Bradfield Bros. Garage $22.50 for gasoline, oil, and storage.
30. Paid secretary's salary for last half of month, $85.
30. Withdrew $200 for personal use.

80 CASH RECEIPTS

DATE		ACCOUNT	DESCRIPTION	POST. REF.	AMOUNT		TOTAL	
			AMOUNTS FORWARDED					
19— Dec.	1		Balance	✓			2929	50
	2	Income from Eng. Fees	Thompson & Whitehead		120	00		
	18	Income from Eng. Fees	The Lacey Mfg. Co.		65	00		
	20	Income from Eng. Fees	Johnson Bros.		250	00		
	28	Income from Eng. Fees	The Brown Trucking Co.		200	00		
					635	00		
	30	Cash Dr.	Total receipts				635	00
							3564	50
							3564	50
Jan.	1		Balance	✓			2917	75

Cashbook for a Personal Service Enterprise (Left-hand page)

It should be remembered that cash transactions only are recorded in a cashbook. Before each transaction is recorded, it is necessary to analyze it to determine whether it represents an increase in cash or a decrease in cash. Increases in cash are recorded on the left-hand or receipts side of the cashbook, while decreases in cash are recorded on the right-hand or payments side. The first transaction of December 1 involved the payment of rent. It had the effect of decreasing cash; therefore it was recorded on the payments side of the cashbook. The transaction of December 2 involved the receipt of cash in payment of engineering fees. It had the effect of increasing cash; therefore it was recorded on the receipts side of the cashbook.

Advantages of the Cashbook. A study of the cashbook reveals that, for the purpose of recording cash receipts and payments, it offers the following advantages over the general journal:

(a) Since one line only is required to record each transaction in the cashbook, there is a saving of time.

(b) Recording cash receipts on the left-hand page and cash payments on the right-hand page of a cashbook facilitates proving the cash balance.

(c) A cashbook makes information more readily available in regard to the total cash receipts, the total cash payments, and the cash balance;

CASH PAYMENTS 81

Date		Account	Description	Post. Ref.	Amount	Total
			Amounts Forwarded			
19— Dec.	1	Rent Expense	Dec. rent		100.00	
	4	Tel. & Tel. Expense	Telephone bill		6.25	
	9	Misc. Expenses	N.A.C.E. dues		15.00	
	12	Donations	Community Chest		15.00	
	15	Accounts Payable	The Williamson Co.		90.00	
	16	Salaries	Secretary's salary		85.00	
	23	Misc. Expenses	Magazine sub.		3.00	
	27	Accounts Payable	Robbins Furn. Co.		25.00	
	29	Auto Expense	Bradfield Bros.		22.50	
	30	Salaries	Secretary's salary		85.00	
	30	M. B. Roberts, Drawing	Personal use		200.00	
					646.75	
	30	Cash Cr.	Total payments			646.75
	30		Balance	✓		2917.75
						3564.50
						3564.50

Cashbook for a Personal Service Enterprise (Right-hand page) it is necessary only to foot the amount columns and to ascertain the difference between the footings to find the cash balance.

(d) A cashbook makes it feasible to employ a bookkeeper to record cash transactions only. This advantage becomes apparent when it is necessary to employ more than one bookkeeper to record all of the transactions of an enterprise.

The use of a cashbook as a book of original entry does not necessarily eliminate the need for using a general journal. There may be some transactions that do not involve the receipt or the payment of cash and that cannot, therefore, be recorded in a cashbook.

For example, if on December 7 M. B. Roberts purchased an adding-listing machine for $150 from the Office Supply Co. on credit, it cannot be recorded in the cashbook because it does not involve the receipt or payment of cash. Neither should it be recorded in the purchases journal which is designed for use in recording merchandise purchases only. It should, therefore, be recorded in the general journal by debiting Office Equipment and by crediting Accounts Payable for $150.

Proving Cash. Cash should be proved frequently. It is customary with most bookkeepers to prove cash before making deposits. Proving cash involves the following procedure:

(a) Ascertaining the total receipts for the period and adding this total to the balance of cash at the beginning of the period. The result is the total amount of cash to be accounted for.

(b) Ascertaining the total payments for the period.

(c) Subtracting the total payments from the sum of (1) the cash balance at the beginning of the period and (2) the total cash receipts for the period. The result is the cashbook balance at the end of the period.

(d) Proving the cashbook balance by counting the undeposited cash on hand and adding it to the amount of the bank balance. The sum of the cash on hand and in the bank should equal the cashbook balance.

Many persons keep a record of deposits and checks issued on the stubs of their checkbooks. If such a record is kept accurately, the bank balance may be ascertained by referring to the checkbook stubs. Some record of the deposits made and of the checks issued should be kept in order that the bank balance may be ascertained readily. If all receipts and payments are properly recorded and the amount columns of the cashbook are footed correctly, the correct cash balance should be indicated. The cash balance may be proved daily, weekly, monthly, or at any time by observing the foregoing procedure.

Cash Over and Short. Cashiers and other employees who are required to handle numerous transactions involving cash find it necessary in some instances to make adjustments for the difference between the total amount of cash they have on hand and the amount they should have on hand. For example, a cashier in a restaurant may handle several hundred transactions in the course of a day. In the process of making change, mistakes may occur. At the end of the day the total cash received should agree with the total of the cash sales tickets issued during the day. If the amount received is more or less than the total of the sales tickets, the discrepancy indicates failure to collect the proper amount of all the sales tickets or mistakes in making change. To facilitate adjustments for such discrepancies, it is customary to keep a *cash over and short* account.

If, in proving cash at the end of the day a shortage of $5 is found, an adjustment may be made by debiting Cash Over and Short and by crediting Cash for the amount of the shortage. Such an adjusting entry may be made on the payments side of the cashbook.

If, instead of a shortage in cash an overage of $5 is found, an adjustment may be made by debiting Cash and by crediting Cash Over and Short for the amount of the overage. Such an adjusting entry may be made on the receipts side of the cashbook.

In no case should such an adjusting entry to record either a shortage or an overage in cash be made (a) until a thorough check has been made to verify the balance of the cash account and the accuracy of the cash count, and (b) until the adjusting entry has been properly authorized.

At the end of an accounting period the balance of the cash over and short account may represent either a loss or a gain. If the account has a debit balance, it represents a loss for the period; if the account has a credit balance, it represents a gain for the period.

Footing, Balancing, and Ruling the Cashbook. Reference to the cashbook reproduced on pages 80 and 81 will reveal that the balance at the beginning of the month, amounting to $2,929.50, is recorded in the Total column on the left-hand page or cash receipts side. It should not be recorded in the Amount column, since that column is used to record the receipts of the month. The procedure in balancing this form of cashbook at the end of the month involves the following steps:

(a) The Amount column on the left-hand side of the cashbook is footed and the footing is recorded in small pencil figures immediately below the horizontal line on which the last entry appears. A single line is then ruled across the Amount column immediately above the footing.

The total receipts are then recorded on the next line by writing the date in the Date column; "Cash Dr." in the Account column; "Total receipts" in the Description column; and the amount in the Total column.

(b) The Amount column on the right-hand side of the cashbook is footed and the footing is recorded in small pencil figures immediately below the horizontal line on which the last entry appears. A single line is then ruled across the Amount column immediately above the footing. The total payments are then recorded on the next line by writing the date in the Date column; "Cash Cr." in the Account column; "Total payments" in the Description column; and the amount in the Total column.

(c) The cashbook balance is then recorded on the next line on the right-hand side of the cashbook by writing the date in the Date column; "Balance" in the Description column; and the amount in the Total column. Most bookkeepers make this entry in red ink. Since this entry is not to be posted, a check mark is entered in the Posting Reference column.

(d) A single line is next ruled across the Total columns on both sides of the cashbook. This ruled line is drawn on the same horizontal line on both pages. The Total columns are then footed, and the footings are recorded in small pencil figures immediately below the single ruled line. If the cashbook is in balance, these footings will be equal. After proving the equality of the footings, the amounts are recorded on the next line.

(e) A double line is then ruled immediately below the totals across all of the columns on both sides of the cashbook, except the Account columns and the Description columns. The double rule indicates that the cashbook is in balance at that point.

(f) The balance is either brought down below the double rule on the cash receipts side or is carried forward to the top of the next cash receipts page and entered in the Total column so that it will not be included in the the receipts for the ensuing month. A check mark is entered in the Posting Reference column to indicate that the item is not to be posted.

Posting from the Cashbook. Posting from the cashbook may be completed daily or periodically. The usual plan is to complete the posting daily, posting the receipts first and the payments second. When transactions have been properly recorded in a cashbook, the information needed for posting purposes is available. For example, refer to M. B. Roberts' cashbook which is reproduced on pages 80 and 81. The December 1 balance is the first item entered on the receipts side. Since this item need not be posted to the cash account, it was checked in the Posting Reference column at the time it was entered.

Each item recorded in the Amount column on the receipts side of a cashbook should be posted to the credit of the account named in the Account column. Each item recorded in the Amount column on the payments side of a cashbook should be posted to the debit of the account named in the Account column. As the posting is completed a proper cross-reference should be provided by entering the page of the cashbook preceded by the letter "C" in the Folio column of the ledger and by entering the page of the ledger in the Posting Reference column of the cashbook. To illustrate the procedure, the accounts with Income from Engineering Fees and Rent Expense are reproduced below. The account with Income from Engineering Fees shows the November 30 balance entered on the credit side followed by the items posted from the receipts side of M. B. Roberts' cashbook. The account with Rent Expense shows the November 30 balance entered on the debit side followed by the item of December 1 posted from the payments side of M. B. Roberts' cashbook.

ACCOUNT *Income from Engineering Fees*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19—					
						Nov.	30	Balance	✓		7458 75
						Dec.	2		C 10		120 00
							18		C 10		65 00
							20		C 10		250 00
							28		C 10		200 00

ACCOUNT *Rent Expense*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19—											
Nov.	30	Balance	✓		1100 00						
Dec.	1		C 11		100 00						

At the end of the month after the Amount columns in the cashbook have been footed and the total receipts and payments determined, the sum of the cash receipts should be posted to the debit of the cash account and the sum of the cash payments should be posted to the credit of the cash account. When posting the receipts it is advisable to write "Total receipts" in the Items column on the debit side of the cash account. When posting the payments it is advisable to write "Total payments" in the Items column on the credit side of the cash account. It will be noted that posting from the cashbook involves both individual and summary posting.

Cashbook of a Merchant. In a cashbook for a merchant who purchases and sells merchandise on credit, it is desirable to provide a special column on the receipts side for Accounts Receivable Cr. and a special column on the payments side for Accounts Payable Dr. It is also advisable to provide special columns for recording net cash receipts and net cash payments. By referring to the cashbook reproduced below, it will be observed that separate columns are provided on the receipts side for recording (a) credits to general ledger accounts, (b) credits to the accounts receivable account, and (c) debits to the cash account. On the payments side separate columns are provided for recording (a) debits to general ledger accounts, (b) debits to the accounts payable account, and (c) credits to the cash account. When this form of cashbook is used, transactions arising from the purchase and the sale of merchandise are recorded in the following manner:

(a) Cash sales are recorded on the cash receipts side of the cashbook by entering the proper amounts in the General Ledger Cr. column and in the Net Cash Received Dr. column.

86 CASH RECEIPTS

Date		Account	Description	Post Ref	General Ledger Cr.	Accounts Receivable Cr.	Net Cash Received Dr.
			Amounts Forwarded				
19— Mar.	1	W. A. Goodrich, Prop.	Investment	5	2000 00		2000 00
	4	Sales	Cash	7	32 00		32 00
	11	Sales	Cash	7	54 00		54 00
	16	Accts. Rec.	A. W. Jordan	✓		16 25	16 25
	18	Sales	Cash	7	84 50		84 50
	25	Accts. Rec.	Peoples Hotel	✓		50 25	50 25
	25	Sales	Cash	7	78 40		78 40
	29	Accts. Rec.	James O'Wills	✓		44 30	44 30
	30	Accts. Rec.	J. C. Wells	✓		26 05	26 05
	31	Sales	Cash	7	57 60		57 60
					2306 50	136 85	2443 35
					(✓)	(2)	(1)
19— Apr.	1		Balance $1,402.50				

Columnar Cashbook for a Mercantile Enterprise (Left-hand page)

(b) Cash receipts from charge customers on account are recorded on the receipts side of the cashbook by entering the proper amounts in the Accounts Receivable Cr. column and in the Net Cash Received Dr. column.

(c) Cash purchases are recorded on the cash payments side of the cashbook by entering the proper amounts in the General Ledger Dr. column and in the Net Cash Paid Cr. column.

(d) Cash payments to creditors on account are recorded on the payments side of the cashbook by entering the proper amounts in the Accounts Payable Dr. column and in the Net Cash Paid Cr. column.

In the preceding unit, the transactions completed by W. A. Goodrich during the month of March were shown recorded in a purchases journal, a sales journal, and a general journal. All of the cash transactions were recorded in a general journal. For comparison, the same cash transactions are recorded in the following columnar cashbook.

Note that Mr. Goodrich's investment of $2,000 on March 1 is recorded on the cash receipts side of the columnar cashbook. A comparison

CASH PAYMENTS 87

DATE		ACCOUNT	DESCRIPTION	POST REF	GENERAL LEDGER DR	ACCOUNTS PAYABLE DR	NET CASH PAID CR
			AMOUNTS FORWARDED				
19— Mar	1	Rent Expense	March	11	95 00		95 00
	2	Purchases	Cash	9	79 30		79 30
	6	Purchases	Cash	9	194 00		194 00
	15	Salaries	Clerks' wages	14	57 50		57 50
	16	Accts. Pay.	King & King	✓		136 95	136 95
	20	Adv. Expense	Newspaper	12	15 00		15 00
	24	Purchases	Freight & drayage	9	27 50		27 50
	27	Purchases	Cash	9	199 10		199 10
	30	Accts. Pay.	Logan Bros.	✓		85 00	85 00
	31	Tel. Expense	March	13	8 00		8 00
	31	Salaries	Clerks' wages	14	57 50		57 50
	31	W. A. Goodrich, Draw.	Personal use	6	80 00		80 00
					812 90	221 95	1034 85

Columnar Cashbook for a Mercantile Enterprise (Right-hand page) of that entry with the first entry in the general journal reproduced on pages 68 and 69 will show that the opening entry to record the proprietor's investment may be made either in a general journal or in a cashbook, with the same results.

It should be noted also that the March 31 cash balance shown in the cashbook reproduced on pages 86 and 87 is the same as the balance of the cash account in Mr. Goodrich's general ledger shown on page 70. Obviously, the cash balance at the end of the month should be the same regardless of whether the cash transactions are recorded in a general journal or in a cashbook.

Transactions recorded in Mr. Goodrich's general journal, reproduced on pages 68 and 69, that do not involve the receipt or the payment of cash are not recorded in the cashbook. Therefore, if Mr. Goodrich were to use the form of columnar cashbook reproduced on pages 86 and 87 in which to record his cash transactions, it would be necessary for him to use a general journal in which to record all transactions that do not pertain to cash or to purchases and sales of merchandise on credit.

Proving the Columnar Cashbook. To prove the columnar cashbook it is necessary only to foot the amount columns on each side and to ascertain that the debit and credit footings on each side are equal in amount. On the receipts side, the sum of the footings of the first two amount columns should equal the footing of the third column. Thus, on March 31 the footings of the amount columns on the receipts side of Mr. Goodrich's cashbook may be proved as follows:

Footing of the General Ledger Cr. column	$2,306.50
Footing of the Accounts Receivable Cr. column	136.85
Total credit footings	$2,443.35
Footing of the Net Cash Received Dr. column	$2,443.35

On the payments side, the sum of the footings of the first two amount columns should equal the footing of the third column. Thus, on March 31 the footings of the amount columns on the payments side of Mr. Goodrich's cashbook may be proved as follows:

Footing of the General Ledger Dr. column	$ 812.90
Footing of the Accounts Payable Dr. column	221.95
Total debit footings	$1,034.85
Footing of the Net Cash Paid Cr. column	$1,034.85

At the time of proving the footings of the columnar cashbook, it is also advisable to prove the cash balance. To ascertain the cash balance, it is necessary to take into consideration (a) the cash balance at the beginning of the month, if any; (b) the net cash receipts for the month; and (c) the net cash payments for the month. Mr. Goodrich's cash balance at the end of March may be ascertained in the following manner:

Net cash receipts for month	$2,443.35
Less net cash payments for month	1,034.85
Cash balance at end of month	$1,408.50

Mr. Goodrich had no cash balance at the beginning of March because he started in business on March 1 with an investment of $2,000, which is included in the net cash receipts for the month.

After ascertaining the balance, it should be recorded on the receipts side of the cashbook in small pencil figures in the Description column immediately below the last regular entry. To prove the cash balance, it is necessary (a) to count the cash and cash items on hand and (b) to ascertain the balance in the bank. When a record of the banking transactions is kept on the checkbook stubs, it is necessary only to refer to the checkbook stub to ascertain the bank balance at any time.

After proving the footings of the columnar cashbook and after proving the cash balance, the columnar totals should be recorded on the same horizontal line on both pages of the cashbook and the book should be ruled with single and double rules as shown in the illustration.

After ruling the cashbook, the balance should be recorded in the Description column on the receipts side on the next horizontal line immediately below the double rules, unless the page is filled, in which case the balance should be recorded at the top of a new page.

Posting from the Columnar Cashbook. Posting from the columnar cashbook involves both individual posting and summary posting. The individual posting is completed daily or periodically, while the summary posting is usually completed at the end of each month.

Individual Posting. In completing the individual posting, each amount entered in the General Ledger Cr. column on the receipts side and in the General Ledger Dr. column on the payments side of the cashbook should be posted individually to the proper accounts. The usual plan is to complete the individual posting from the receipts side first. As each item is posted, the ledger folio should be entered in the Posting Reference column of the cashbook.

Individual ledger accounts may or may not be kept with customers and with creditors. Posting may be done from the books of original entry or directly from vouchers or other business forms representing the transactions. Since Mr. Goodrich does not keep individual ledger accounts with customers and with creditors, no individual posting from the Accounts Receivable Cr. and Accounts Payable Dr. columns of his cashbook is required. The check marks appearing in the Posting Reference columns of Mr. Goodrich's cashbook were made at the time of recording such transactions and serve to indicate that these items are not to be posted individually.

Summary Posting. The summary posting from a columnar cashbook should be completed as follows:

(a) The total of the Accounts Receivable Cr. column should be posted to the credit of Accounts Receivable.

(b) The total of the Net Cash Received Dr. column should be posted to the debit of Cash.

(c) The total of the Accounts Payable Dr. column should be posted to the debit of Accounts Payable.

(d) The total of the Net Cash Paid Cr. column should be posted to the credit of Cash.

ACCOUNT Cash — Page 1

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Mar.	31	Total Receipts 1,408.50	C86		2,443.35	19– Mar.	31	Total Payments	C87		1,034.85

ACCOUNT Accounts Receivable — Page 2

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Mar.	31	Total Charge Sales [illegible]	S67		653.46	19– Mar.	7		J68		9.10
							31		C86		1,368.85

ACCOUNT Accounts Payable — Page 4

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Mar.	18		J68		12.60	19– Mar.	4		J68		185.00
	30		J69		4.00		31	Total Cr. Purchases [illegible]	P67		434.45
	31		C87		224.95 [illegible]						

To indicate that the summary posting of a column has been completed, the ledger folio should be entered immediately below the total as a posting reference. Check marks may be placed immediately below the totals of the General Ledger columns to indicate that the totals need not be posted. To illustrate the posting procedure, the posting references were inserted in the cashbook reproduced on pages 86 and 87. The accounts affected by the summary posting are reproduced on page 90. All of the other accounts that were affected by the individual posting only are reproduced on pages 70 to 72.

The use of a special column for Accounts Receivable Cr. on the receipts side of the cashbook saves time since it is then unnecessary to post each item individually to the credit of the accounts receivable account in the general ledger. Likewise, the use of a special column for Accounts Payable Dr. on the payments side of the cashbook makes it unnecessary to post each item individually to the debit of the accounts payable account in the general ledger.

A comparison of the accounts reproduced on page 90 with the same accounts appearing on pages 70 and 71 will reveal the time-saving feature of summary posting as compared with individual posting.

PRACTICE ASSIGNMENT No. 7. Complete Report No. 7 in the workbook and submit your working papers to the instructor for approval. After completing the report, continue with the following study assignment until Report No. 8 is required.

VIII THE COMBINED CASH-JOURNAL

A *combined cash-journal* is a book of original entry combining features of both the general journal and the cashbook. Because it is easy to use and is self-balancing, the combined cash-journal is a popular type of book of original entry that is widely used in personal service and retail merchandising enterprises. A combined cash-journal may be proved at any time merely by footing the amount columns and by comparing the sum of the debit footings with the sum of the credit footings.

Form of Combined Cash-Journal. A combined cash-journal may be a bound book or a loose-leaf book. The blankbook manufacturers produce cash journals with a variety of amount columns, with or without printed headings. Public accountants frequently design cash journals to fit the needs of particular enterprises. In selecting a form of combined cash-journal for a particular enterprise, an effort should be made to obtain the desired number of amount columns to fit the needs of the enterprise.

For a mercantile enterprise that buys and sells merchandise on credit, the simplest form of combined cash-journal that is satisfactory is one similar to that illustrated on page 93. Standard eight-column paper is used in that journal. The Description column should be used to record the account titles affected by the amounts entered in the General Dr. and Cr. columns. Descriptive information, such as the names of individuals or firms, check numbers, credit memorandum numbers, etc. may also be recorded in this column. The account titles should be written at the left of the column, followed by the descriptive information. When an entry is supported by a proper voucher or document, little descriptive information need be recorded since the number of the voucher or document should provide a satisfactory cross reference.

The two amount columns at the left of the Description column are used in recording cash receipts and cash disbursements. All cash receipts should be recorded in the Dr. column and all cash disbursements should be recorded in the Cr. column. These columns serve the same purpose as a cashbook in which receipts are recorded on the left-hand page and disbursements are recorded on the right-hand page.

The first two amount columns at the right of the Description column are used to record transactions that are to be posted individually to accounts kept in the general ledger. In recording such transactions, the proper account title should be recorded in the Description column and the correct amount should be entered in the proper Dr. or Cr. column. These columns serve the same purpose as an ordinary two-column general journal.

The second pair of amount columns at the right of the Description column are used to record transactions affecting the accounts receivable account, debits being recorded in the left-hand amount column and credits in the right-hand amount column.

The last two amount columns are used to record transactions affecting the accounts payable account, debits being recorded in the left-hand amount column and credits in the right-hand amount column.

A Combined Cash-Journal Illustrated. The combined cash-journal illustrated on page 93 was used to record the transactions completed by W. A. Goodrich during the month of March. A narrative of the transactions appears on pages 64 to 66 of Unit Two. When a combined cash-journal is used in conjunction with a purchases journal and a sales journal, all transactions involving the purchase of merchandise on credit should

COMBINED CASH-JOURNAL FOR MONTH OF March 19— 93

Cash Receipts Dr.	Cash Payments Cr.	Date Mo.	Date Day	Description	Post. Ref.	General Debits	General Credits	Accounts Receivable Debits	Accounts Receivable Credits	Accounts Payable Debits	Accounts Payable Credits
				AMOUNTS FORWARDED							
2000 00		Mar.	1	W. A. Goodrich, Proprietor			2000 00				
	95 00		1	Rent Expense		95 00					
	79 30		2	Purchases; Brown Bros.		79 30					
			4	Store Equipment–Logan Bros.		185 00					185 00
32 00			4	Sales; sundry cash			32 00				
	194 00		6	Purchases; Brown Bros.		194 00					
			7	Sales R.&A.–Peoples Hotel		9 10			9 10		
54 00			11	Sales; sundry cash			54 00				
	57 50		15	Salaries		57 50					
16 25			16	A. Y. Jordan	✓				16 25		
	136 95		16	King & King	✓					136 95	
			18	King & King–Pur. R.&A.			12 60			12 60	
84 50			18	Sales; sundry cash			84 50				
	15 00		20	Advertising Expense		15 00					
	27 50		24	Purchases; freight & drayage		27 50					
50 25			25	Peoples Hotel	✓				50 25		
78 40			25	Sales; sundry cash			78 40				
	199 10		27	Purchases; Brown Bros.		199 10					
44 30			29	James O. Wills	✓				44 30		
26 05			30	J. C. Wells	✓				26 05		
	85 00		30	Logan Bros.	✓					85 00	
			30	Lake View Creamery–Pur. R.&A.			4 00			4 00	
57 60			31	Sales; sundry cash			57 60				
	8 00		31	Telephone Expense		8 00					
	57 50		31	Salaries		57 50					
	80 00		31	W. A. Goodrich, Drawing $1,408.50		80 00					
2443 35	1034 85					1007 00	2323 10		145 95	238 55	185 00
		Apr.	1	Balance, $1,408.50							

Combined Cash-Journal for a Mercantile Enterprise be recorded in the purchases journal, all transactions involving the sale of merchandise on credit should be recorded in the sales journal, and all other transactions should be recorded in the combined cash-journal.

In analyzing Mr. Goodrich's combined cash-journal for March, it will be noted that each transaction is recorded on one horizontal line. Check marks have been placed in the Posting Reference column in those entries where individual posting is not required from the General Dr. or Cr. columns. For example, the first transaction of March 16 is recorded as a debit to Cash and a credit to Accounts Receivable. Since there are no entries in the General Dr. or Cr. columns to be posted individually, a check mark was placed in the Posting Reference column.

Proving a Combined Cash-Journal. To prove a combined cash-journal, it is necessary to foot all of the amount columns and to compare the sum of the debit footings with the sum of the credit footings. The footings should be proved frequently; when the transactions are numerous, it may be advisable to prove the footings daily. Usually, however, it will be sufficient to prove the footings at the end of each week. Some bookkeepers follow the practice of proving the footings before making each bank deposit. The following is a proof of the footings of Mr. Goodrich's combined cash-journal at the end of March:

PROOF OF COMBINED CASH-JOURNAL FOOTINGS,
MARCH 31, 19--

Column Heading	Dr.		Cr.	
Cash	2,443	35	1,034	85
General	1,007	00	2,323	10
Accounts Receivable			145	95
Accounts Payable	238	55	185	00
	3,688	90	3,688	90

At the time of proving the footings of the combined cash-journal, it is advisable also to prove the cash balance. To prove the cash balance, it is necessary to count the cash and cash items on hand; also to ascertain the balance in the bank. When a record of the banking transactions is kept on the checkbook stub, it is necessary only to refer to the checkbook stub to ascertain the bank balance at any time.

A proof of Mr. Goodrich's cash balance at the end of March appears at the top of the following page.

PROOF OF CASH BALANCE, MARCH 31, 19--

Cash receipts for month	$2,443.35
Less cash payments for month	1,034.85
Cash balance at end of month	$1,408.50
Cash on hand	None
Bank balance per checkbook stub	$1,408.50

The reason there was no cash on hand at the end of the month was because all cash received during the month had been deposited in the bank, the last deposit having been made on March 31.

Footing and Ruling a Combined Cash-Journal. A combined cash-journal should be footed and ruled at the end of each month. The footings should first be recorded in small pencil figures immediately below the last regular entry. After being proved, the totals should be recorded in ink on the next horizontal line, unless the page is filled, in which case the totals should be recorded on the double ruled line at the bottom of the page. If the page is not filled, a single rule should be drawn across all of the amount columns just above the totals and a double rule should be drawn across all of the columns except the Description column, just below the totals.

The cash balance at the beginning of the month should be recorded in the Description column. Inasmuch as Mr. Goodrich started in business on March 1, there was no beginning balance to be recorded on that date. At the end of the month, the cash balance should be ascertained by adding the total receipts for the month to the beginning balance and by subtracting the total payments for the month. This balance should be recorded in small pencil figures in the Description column immediately below the last regular entry. The April 1 balance should be entered in the Description column before recording any transactions for April.

When it is necessary to carry forward the totals of a page of a combined cash-journal, each column should be footed and the footings should be proved by ascertaining the equality of the debits and credits. After the footings have been proved, the totals should be recorded in ink and the words "Carried Forward" should be written in the Description column. The totals should then be recorded at the top of the next page by writing the words "Amounts Forwarded" in the Description column and by entering the correct total in each amount column.

Posting from a Combined Cash-Journal. Posting from a combined cash-journal involves both individual posting and summary posting. The individual posting is completed daily or periodically while the summary posting is usually completed at the end of each month.

Individual Posting. In completing the individual posting from Mr. Goodrich's combined cash-journal, each item recorded in the General columns should be posted to the proper account in the general ledger. The account title appears at the left in the Description column. Each item recorded in the left-hand General column should be posted to the debit of the account affected, while each item recorded in the right-hand General column should be posted to the credit of the account affected. Thus, in posting the first entry of March 1, the account of W. A. Goodrich, Proprietor, should be credited for $2,000. The ledger folio should be entered in the Posting Reference column of the combined cash-journal and the combined cash-journal folio should be entered in the Folio column of the ledger account to provide a suitable cross reference.

It may or may not be necessary to post individually the amounts entered in the Accounts Receivable Dr. and Cr. columns and the Accounts Payable Dr. and Cr. columns. This will depend upon whether or not individual ledger accounts are kept with customers and with creditors and whether or not the posting is done from the books of original entry or directly from vouchers or other business forms representing the business transactions. Since Mr. Goodrich does not keep individual ledger accounts with customers and with creditors, no individual posting from these columns of his combined cash-journal is required.

Summary Posting. The totals of all of the amount columns in Mr. Goodrich's combined cash-journal, except the General Dr. and Cr. columns, should be posted to the accounts named in the headings of the columns. This summary posting should be completed after all the amount columns have been footed, the debit and credit footings proved, the totals entered, and the ruling completed. The summary posting from Mr. Goodrich's combined cash-journal should be completed in the following order:

(a) Post the total of the Cash Receipts Dr. amount column to the debit of Cash.

(b) Post the total of the Cash Payments Cr. amount column to the credit of Cash.

(c) Post the total of the Accounts Receivable Dr. amount column to the debit of Accounts Receivable.

(d) Post the total of the Accounts Receivable Cr. amount column to the credit of Accounts Receivable.

(e) Post the total of the Accounts Payable Dr. amount column to the debit of Accounts Payable.

(f) Post the total of the Accounts Payable Cr. amount column to the credit of Accounts Payable.

As the total of each amount column is posted, the ledger folio should be entered immediately below the total as a posting reference. Check marks may be placed immediately below the totals of the General Dr. and Cr. amount columns to indicate that these totals need not be posted.

After completing the summary posting from all of Mr. Goodrich's books of original entry, including the purchases journal, the sales journal, and the combined cash-journal, the accounts receivable and accounts payable accounts appeared as follows:

ACCOUNT *Accounts Receivable*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar.	31	507.51	S67		653 46	19— Mar.	31		CJ93		145 95

ACCOUNT *Accounts Payable*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Mar.	31		CJ93		238 55	19— Mar.	31		P67		434 45
							31	[illegible]	CJ93		[illegible]

The accounts receivable account was debited for the total credit sales for March, the amount being posted from the sales journal. The account was credited for the total payments received from customers during March, the amount being posted from the combined cash-journal. The balance of the account amounting to $507.51 represents the amount due from customers at the end of the month.

The accounts payable account was debited for the total payments made to creditors during March, the amount being posted from the combined cash-journal. The account was credited for the total amount of merchandise purchased on credit during the month, the amount being posted from the purchases journal. The account was also credited for the sum of all invoices received during the month representing the purchase on credit of property other than merchandise, the amount being posted from the combined cash-journal. The balance of the account amounting to $380.90 represents the amount owed to creditors at the end of the month. By comparing the foregoing accounts with the corresponding accounts in Mr. Goodrich's ledger reproduced on pages 70 and 71, it will be seen that the use of a combined cash-journal resulted in a saving of time in posting due to the summary posting. It will also be noted that the balances of the accounts are the same in both illustrations.

PRACTICE ASSIGNMENT No. 8. Refer to the workbook and complete Report No. 8. If you have studied the first three units of this textbook and have a clear understanding of the principles developed therein, you should experience no difficulty in completing the workbook assignment. After completing the report, you may proceed with the textbook discussion in Unit Four until the next report is required.

Unit Four

BANKING AND PETTY CASH TRANSACTIONS

IX ACCOUNTS WITH THE BANK

A bank is a financial institution that receives deposits, lends money, makes collections, and renders other services, such as providing vaults for the safekeeping of money, securities, and other valuables, or handling trust funds for its customers. Most banks solicit both checking accounts and savings accounts.

Checking Account. A checking account is sometimes referred to as a commercial account. Important factors in connection with a checking account are (a) opening the account, (b) making deposits, (c) making withdrawals, and (d) reconciling the bank balance.

Opening a Checking Account. To open a checking account with a bank, it is necessary to obtain the approval of an official of the bank and to make an initial deposit. Money, checks, bank drafts, money orders, and other cash items will usually be accepted for deposit. Cash is accepted for deposit subject to verification as to amount and validity. Cash items are accepted for deposit subject to their being paid (honored) by their makers when presented for payment by the bank or its agent.

Signature Card. Banks usually require a new depositor to sign his name on a *signature card* or form as an aid in verifying the depositor's signature on checks that he may issue, on cash items that he may endorse for deposit, and on other business papers that he may present to the bank. One form of signature card is shown in Illustration No. 5. If desired, a depositor may authorize others to sign his name to checks and to other business forms. Each person who is so authorized is required to sign the depositor's name along with his own signature on a signature card. A signature card is one of the safeguards that a bank uses to protect its own interests as well as the interests of its depositors.

AUTHORIZED SIGNATURE FOR

LIBERTY NATIONAL BANK

In receiving items for deposit or collection, this bank acts only as depositor's collecting agent and assumes no responsibility beyond the exercise of due care. All items are credited subject to final payment in cash or solvent credits. This bank will not be liable for default or negligence of its duly selected correspondents nor for losses in transit, and each correspondent so selected shall not be liable except for its own negligence. This bank or its correspondents may send items directly or indirectly to any bank including the payer, and accept its drafts or credit as conditional payment in lieu of cash; it may charge back any item at any time before final payment, whether returned or not, also any item drawn on this bank not good at close of business on day deposited.

SIGNATURE W. L. Mann

ADDRESS 17 N. Third St.

INTRODUCED BY

DATE Oct. 1, 19— H. D. Cull

Illustration No. 5, Signature Card

Deposit Ticket. The bank provides a blank deposit ticket on which the depositor is required to list the items that are being deposited. A model filled-in deposit ticket is reproduced in Illustration No. 6.

In preparing a deposit ticket, the name of the depositor and the date should be written in the spaces provided for these purposes. Coins, including pennies, nickels, dimes, quarters, half dollars, and silver dollars, that are to be deposited in considerable quantities should be wrapped in coin wrappers, which the bank will provide. The name of the depositor should be written on the outside of each coin wrapper as a means of identification in the event that a mistake has been made in counting the coins. Paper money should be arranged in the order of the denominations, the smaller denominations being placed on top. The amounts of cash represented by paper money (currency) and by coins should be entered in the amount column of the deposit ticket on the lines provided for these items.

Each additional item to be deposited should be listed on a separate line of the deposit ticket as shown in Illustration No. 6. In listing checks on the deposit ticket, the instructions of the bank should be observed in describing the checks for identification purposes. Formerly it was common practice to list local checks by name of bank and out-of-town checks by name of city. Currently the preferred practice is to identify each check by entering the American Bankers Association (A.B.A.) transit number on the deposit ticket.

LIBERTY NATIONAL BANK

BY W. L. Mann

October 21 19—

CURRENCY		340	00
COIN		30	94
CHECKS	13-1	217	60
	13-32	500	00
	13-3	150	00
	TOTAL $	1,247	54

PLEASE LIST EACH CHECK SEPARATELY

Illustration No. 6, Deposit Ticket

The A.B.A. numbers usually appear on checks as shown in Illustration No. 7. The numerator of the fraction is the transit number, while the denominator is the routing symbol. Such identification numbers are assigned to banks by the American Bankers Association. Numbers 1 to 49 are assigned to large cities and numbers 50 to 99 are assigned to the states. Number 13 appearing on the check shown in Illustration No. 7 is the number assigned to Cincinnati, Ohio, while 1 is the number assigned to the First National Bank.

There are twelve Federal Reserve Bank Districts. Cincinnati is located in the 4th District. If the denominator has three digits, the first digit designates one of the Federal Reserve Districts numbered 1 to 9. The second digit designates the Federal Reserve Bank or Branch serving the territory in which the drawee bank is located. If a bank is located in a city where the head office of the Federal Reserve Bank is located, this fact will be indicated by the figure 1. Branches of the Federal Reserve Bank arranged alphabetically are designated by figures 2 to 5. Thus, the first two digits of number 420 indicate that the First National Bank, Cincinnati, Ohio, is located in the 4th Federal Reserve District and that Cincinnati is served by Branch No. 2 of the Federal Reserve Bank.

The third digit of the denominator serves two purposes: first, it facilitates the separation of items that are receivable for immediate credit from those that are receivable for deferred credit, and second, it facilitates the sorting of items by states in any case where that is convenient. Figure 0 designates items that are receivable for immediate credit if received in time to be cleared on the current day. All other figures designate items that are receivable for deferred credit, and also designate the state in which the drawee bank is located.

When a bank is located in one of those Federal Reserve Districts that is numbered 10 to 12, the denominator will have four digits, the first two of which designate the Federal Reserve District in which the bank is located.

Many banks provide special envelopes for the use of depositors in depositing bond coupons. Only one kind of coupon should be placed in each envelope and the amount of the coupons placed in each envelope should be listed separately on the deposit ticket. Thus, if two U. S. Government Bond coupons valued at $12.50 each are being deposited, they should be enclosed in the envelope provided for that purpose and the total should be listed on the deposit ticket as "U. S. Bond Coupons, $25." If, at the same time, a coupon from an industrial bond is being deposited, it should be placed in a separate envelope.

Endorsements. Items requiring endorsements should be endorsed on the back by the depositor, except postal money orders, which provide space for endorsements on the front. Negotiable instruments such as checks, notes, and drafts, made payable to the depositor either directly or by prior endorsement, must be endorsed by him before a bank will accept them for deposit. One purpose of such endorsement is to transfer the title of the instrument to the bank. By means of his endorsement the depositor also guarantees the payment of the instrument. Checks and other items submitted for deposit that require endorsements on the back may be endorsed as shown in Illustration No. 7. In endorsing a check, the name of the payee should be written exactly as it appears on the face of the check. Note that the endorsement is written near the left end of the check. The left end is the end that is at the left when the front of the check is held in position for reading. This form of endorsement is known as a restrictive endorsement. When so endorsed a check cannot be cashed by anyone other than the bank to whom it is endorsed.

The total of the cash and other items deposited should be entered on the deposit ticket. The deposit ticket, together with the cash and the other items to be deposited, should be delivered to the receiving teller of the bank. The teller may enter the date and the amount of the deposit in a passbook that is provided by the bank. If the passbook is not available when a deposit is being made, the deposit ticket may be prepared in duplicate; the teller will receipt the duplicate copy and return it to the depositor to be retained by him until such time as it is convenient to enter the amount of the deposit in his passbook.

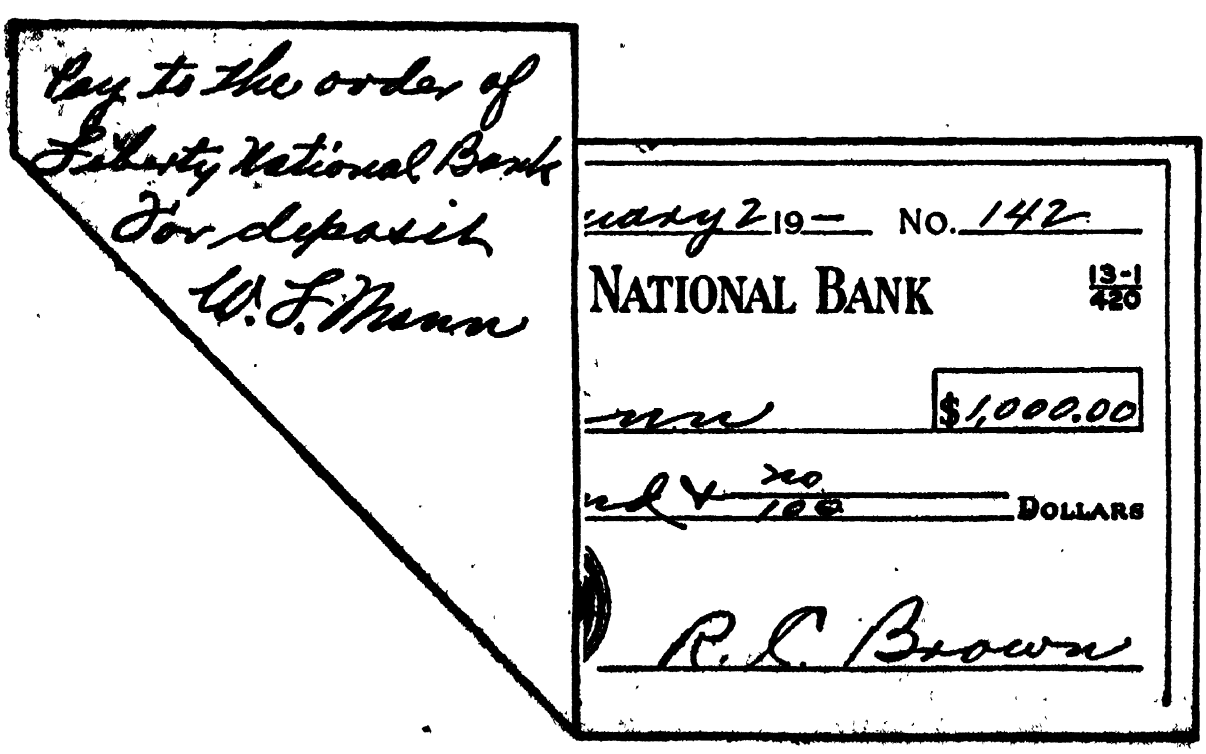


Illustration No. 7, Endorsement for Deposit

Instead of providing the depositor with a passbook, the bank may provide the depositor with a machine-printed receipt for each deposit. Some banks use *automatic teller machines* in preparing the receipts. The use of such machines saves the time of making hand-entries in a passbook and eliminates any need for making duplicate copies of deposit tickets. Such machines not only are time-saving machines, but they also promote accuracy in the handling of deposits. The deposits handled by each teller during the day may be accumulated so that at the end of the day the total amount of the deposits received by a teller is automatically recorded by the machine and this amount may be proved by counting the cash and cash items accepted for deposit during the day.

Dishonored Checks. Under banking customs the depositor guarantees all items that he deposits and is liable to the bank for the amount involved if, for any reason, any item is not honored when presented for payment. When a check or other cash item is deposited with a bank and is not honored upon presentation to the bank upon which it is drawn, the depositor's bank may charge the amount of the dishonored item to the depositor's account or present it to the depositor for reimbursement. It is not uncommon for checks that have been deposited to be returned to the depositor for various reasons, as indicated on the return notice reproduced in Illustration No. 8. The most common reason why checks are returned unpaid is "not sufficient funds" (N.S.F.).

Under the laws of most states, it is illegal for anyone to issue a check on a bank without having sufficient funds on deposit with that bank to redeem the check when it is presented for payment. When a *dishonored check* is charged to the depositor's account, or is redeemed by the depositor

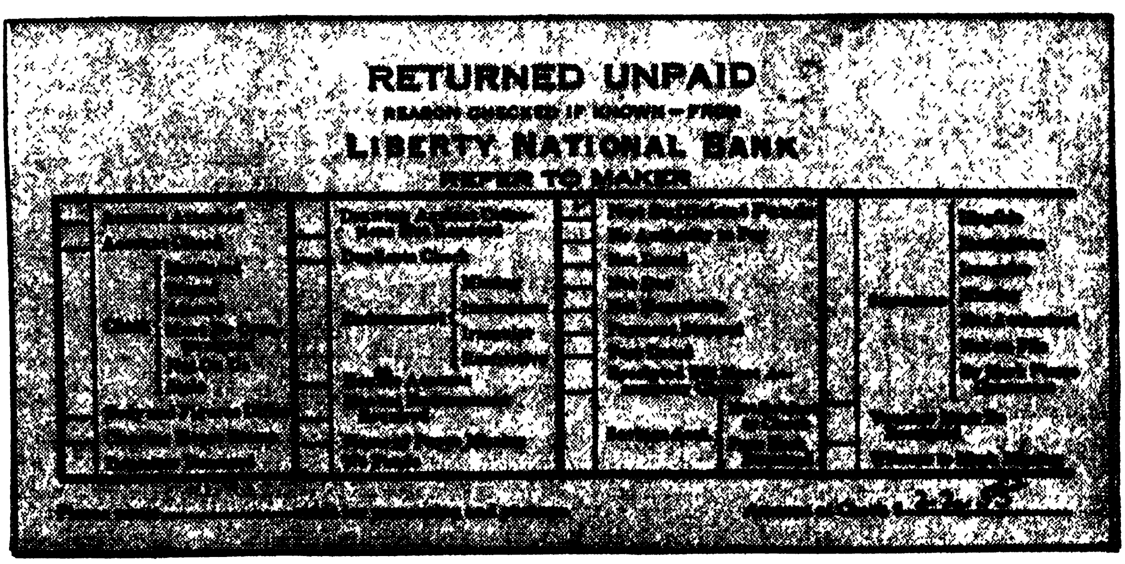


Illustration No. 8, Return Notice

issuing his own check, an entry should be made in the cashbook debiting the maker of the dishonored check and crediting Cash. If the depositor issues his own check to reimburse the bank, it should be recorded on his checkbook stub. If the dishonored check is charged to the depositor's account by the bank, the depositor should deduct the amount from the balance shown on his checkbook stub, even though he did not issue a check.

Postdated Checks. Sometimes *postdated checks* are issued; that is, they are dated subsequent to the date of issue. Thus, a check issued on March 1 may be dated March 15. The recipient of a postdated check should not deposit it before the date specified on the check. One reason for issuing a postdated check may be that the maker does not have sufficient funds in his bank at the time of issuance to pay it, but he may expect to have a sufficient amount on deposit by the time the check is presented for payment on or after the date of the check. When a postdated check is

(TEAR OFF HERE AND ENCLOSE IN ATTACHED ENVELOPE WITH YOUR DEPOSIT)

W. L. Mann
12 N. Third St.
Cincinnati, Ohio

YOUR NAME AND ADDRESS ON THESE LINES. ☞

DIRECTIONS FOR BANKING BY MAIL
1. Fill out attached deposit slip. Write name at the top exactly as account is carried on our books.
2. Endorse checks as follows: Pay to the order of Liberty National Bank (Your Signature.)
3. Enclose checks etc. in pocket of envelope, seal, stamp and mail.
4. Send currency by registered mail.
5. For duplicate record of deposit, put carbon paper between deposit slip and back of deposit receipt.

MAIL DEPOSIT RECEIPT

We credit your checking account this day, as per name and address below with $

LIBERTY NATIONAL BANK

by

MAIL DEPOSIT SLIP

Deposited With

LIBERTY NATIONAL BANK

May 15 19—

Please See That All Checks Are Properly Endorsed

	DOLLARS	CENTS
CURRENCY—Please Send by Registered Mail		
CHECKS—Please List Separately With Name of Bank or Place Drawn On.		
13-1	29	50
13-32	136	45
56-29	16	25
32-10	225	00
86-1248	8	75
60-383	29	60
60-131	142	10
TOTAL	587	65

Name W. L. Mann
12 N. Third St.
Address Cincinnati, Ohio

Illustration No. 9, Mail Deposit Slip

presented to the bank on which it is drawn and payment is not made, it is handled by the bank in the same manner as any other dishonored check and the payee should handle it as he would any other dishonored check.

Making Deposits by Mail. Bank deposits may be made either over the counter or by mail. The over-the-counter method of making deposits is generally used. It may not always be convenient, however, for a depositor to make his deposits over the counter, especially if he lives at a great distance from the bank. In such a case it may be more convenient for him to make his deposits by mail. When a depositor makes his deposits by mail, the bank may provide him with a special form of deposit ticket similar to that shown in Illustration No. 9.

Night Deposits. A depositor may find it convenient to use the night deposit safe of his bank. The opening to the night deposit safe is on the exterior of the bank building. Upon signing a night depository contract, the bank supplies the depositor with a key to the door in the opening of the safe, together with a bag that has an identifying number and in which valuables may be placed and duplicate keys to the bag itself. Once the depositor places his bag in the night deposit safe it cannot be retrieved because it gravitates to a vault in the bank that is accessible to bank employees only. Since only the depositor is provided with keys to his bag, he or his authorized representative must go to the bank to unlock the bag. The depositor may or may not subsequently deposit in his account in the bank the funds that he has placed temporarily in the night deposit safe.

Night deposit banking service is especially valuable to those individuals and concerns that do not have safe facilities in their own places of business and that accumulate cash and other cash items which they cannot take to the bank during banking hours.

Making Withdrawals. The amount deposited in a bank checking account may be withdrawn either by the depositor himself or by any other person who has been properly authorized to make withdrawals from the depositor's account. Such withdrawals are effected by signatures identical with those on the depositor's signature card.

Checkbook. Banks provide printed forms known as checks for the convenience of their depositors. Such checks are used by depositors to authorize the bank to pay out specified amounts from the funds credited to their accounts. Special forms of checks may be provided for pay rolls, dividends, or other purposes. Voucher checks are used by many firms.

Blank checks are usually bound in a book with one or more checks to a page. Each check usually contains spaces for recording the following information:

(a) The number of the check.
(b) The date of the check.
(c) The name of the payee.
(d) The amount the bank is authorized to pay the payee.
(e) The signature of the drawer — the depositor or his authorized agent.

The stub of a checkbook usually contains blank spaces for recording the same information that is recorded on the checks issued; thus the completed stubs provide the depositor with a record of all checks issued. Sometimes blank space is also provided on the stub of each check for recording the title of the account to be debited. In any event, sufficient data should be entered on the stub of each check to provide the information needed for recording purposes. Checks should be numbered consecutively, and their stubs should bear identical numbers. The numbers may be penwritten or a numbering machine may be used. It is a good plan to number all stubs and checks before any checks are issued. Frequently banks provide checkbooks and stubs already numbered and with the name and address of the depositor printed on the checks in accordance with the directions of the depositor.

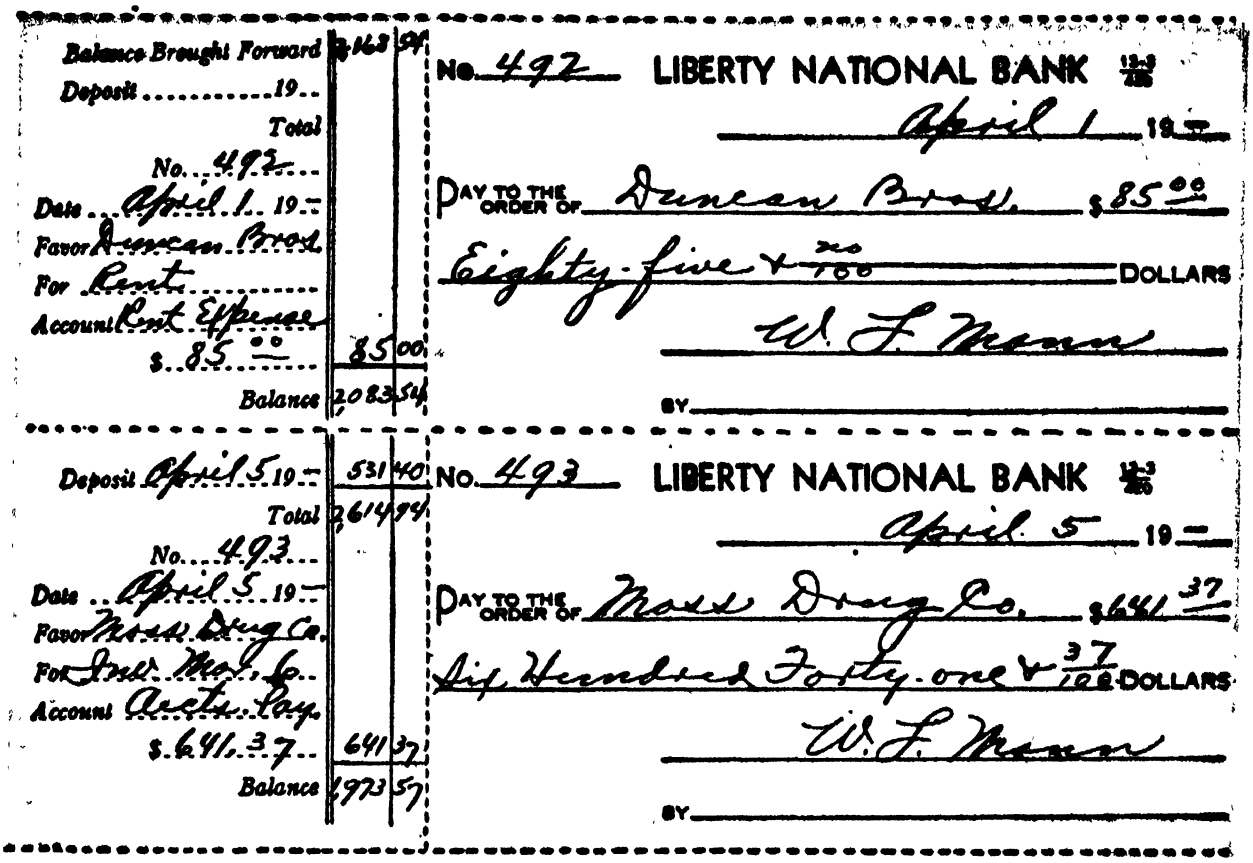
Writing a Check. The stub should be filled in before the check is written. This plan insures the drawer a record of each check issued.

When a depositor withdraws funds personally, the payee of the check should be designated as "Myself," "Cash," "Pay Roll," "Postage Stamps," or the like. Any one of the foregoing terms will indicate that the check is to be cashed at the bank for a special purpose.

When a depositor desires the bank to pay the money to a third party, he writes the name of that party, referred to as the payee, on the stub and on the check. When the payee presents the check to the bank for payment, he may be required by the bank to identify himself.

The purpose for which a check is drawn is usually recorded on the stub below the name of the payee. The purpose may also be indicated in the lower left-hand corner of the check. Indicating the purpose on the check provides information for the benefit of the payee and provides a specific receipt for the drawer.

The amount is stated on the stub in figures and is stated on the check in both figures and words. If the amount shown on the check in figures does not agree with the amount shown in words, the bank usually will return the check unpaid. (See Illustration No. 8).



Balance Brought Forward 2168 94
Deposit ....19..
Total
No. 492
Date April 1. 19
Favor Duncan Bros.
For Rent
Account Rent Expense
$ 85.00 85 00
Balance 2083 54

No. 492 LIBERTY NATIONAL BANK
April 1 19
PAY TO THE ORDER OF Duncan Bros. $85.00
Eighty-five + no/100 DOLLARS
W. F. Mann
BY

Deposit April 5 19 531 40
Total 2614 94
No. 493
Date April 5. 19
Favor Moss Drug Co.
For Inv. Mar. 6
Account Accts. Pay.
$ 641.37 641 37
Balance 1973 57

No. 493 LIBERTY NATIONAL BANK
April 5 19
PAY TO THE ORDER OF Moss Drug Co. $641.37
Six Hundred Forty-one + 37/100 DOLLARS
W. F. Mann
BY

Illustration No. 10, Checks and Stubs

Care must be used in writing the amount on the check in order to avoid any possibility that the payee or a subsequent holder may change the amount. If the instructions given below are followed in the preparation of a check, it will be difficult to change the amount.

(a) The amount stated in figures should be written immediately at the right of the dollar sign on the check so that space for another figure is not left between the dollar sign and the first figure in the amount.

(b) The amount stated in words should be written beginning at the extreme left on the line provided for this information.

(c) The cents should be written in the form of a common fraction; if the check is for an even number of dollars, use two ciphers or the word "no" as the numerator of the fraction.

(d) A line should be drawn from the amount stated in words to the word "Dollars" on the same line with it, as shown in Illustration No. 10.

Frequently a machine known as a *check writer* is used to write the amount of a check in figures and in words. The use of a check writer is desirable because it practically eliminates the possibility of a change in the amount of a check.

Each check issued by a depositor will be returned to him by the bank on which it is drawn after the check has been paid. Canceled checks are returned to the depositor with the bank statement, which is usually rendered each month. All canceled checks will be endorsed by the payee and any subsequent holders. Canceled checks constitute receipts that the depositor should retain for future reference. They may be pasted to the stubs from which they were removed originally or they may be filed.

Overdraft. As stated previously, it is illegal in most states for a depositor to issue a check against a bank in excess of the amount on deposit. However, it may happen that through an oversight or an error in calculation a depositor will overdraw his checking account. Should this happen the bank may refuse to honor the check or it may honor the check and notify the depositor that he has overdrawn his account. In Illustration No. 11 is shown a form that may be used for this purpose. Sometimes an official of the bank will telephone the depositor instead of notifying him by mail. Overdrawing a bank checking account is considered a serious matter and the depositor is expected to make the necessary adjustment without delay.

LIBERTY NATIONAL BANK $\frac{13\text{-}3}{420}$

September 18, 19—

According to our records your account is overdrawn $28.10

If this does not agree with your record, will you please contact us at once in order that any error which may have occurred may be adjusted.

Otherwise, we shall appreciate having you deposit sufficient funds to cover the overdraft as soon as possible.

Your prompt attention is appreciated.

W. L. Mann

12 N. Third St.

Cincinnati, Ohio

Illustration No. 11, Notice of Overdraft

Recording Bank Transactions. A depositor should keep a record of the transactions he completes with his bank. The usual plan is to keep this record on the checkbook stubs as shown in Illustration No. 10. It will be noted that the record consists of detailed information concerning each check written and an amount column in which should be recorded (a) the balance brought forward or carried down, (b) the amount of deposits to be added, and (c) the amount of checks to be subtracted. The purpose is to keep a detailed record of deposits made and checks issued and to indicate the balance in the checking account after each check is drawn.

As the amount of each check is recorded in the cashbook, a check mark may be placed immediately after the account title written on the stub to indicate that it has been recorded. When the canceled check is subsequently received from the bank, the amount shown on the stub may be checked to indicate that the canceled check has been received.

Records Kept by a Bank. The usual transactions completed by a bank with a depositor are:

(a) Accepting deposits made by the depositor.
(b) Paying checks issued by the depositor.
(c) Lending money to the depositor.
(d) Discounting commercial paper for the depositor.
(e) Collecting the amounts of various kinds of commercial paper, such as notes and drafts, for the account of the depositor.

The bank keeps an account with each depositor. Each transaction affecting a depositor's account is recorded by debiting or crediting his account, depending upon the effect of the transaction. When a bank accepts a deposit, the account of the depositor is credited for the amount of the deposit.

When the bank pays a check that has been drawn on the bank, it debits the account of the depositor for the amount of the check. If the bank makes a collection for a depositor, the net amount of the collection is credited to his account. At the same time the bank notifies the depositor on a form similar to the one shown in Illustration No. 12 that the collection has been made.

Bank Statement of Account. Usually at the end of each month a bank renders a statement of account to each depositor similar to that shown in Illustration No. 13. This statement is a report showing (a) the balance on deposit at the beginning of the month, (b) the amounts of deposits made

CREDIT ADVICE

LIBERTY NATIONAL BANK

To W. L. Mann, 12 N. Third St., Cincinnati, Ohio

WE HAVE CREDITED YOUR ACCOUNT AS FOLLOWS:			
Check - Griffin, Ga.		250	00
	Cost		30
		249	70

In receiving items for deposit or collection, this bank acts only as depositor's collecting agent and assumes no responsibility beyond the exercise of due care. All items are credited subject to final payment in cash or solvent credits. This bank will not be liable for default or negligence of its duly selected correspondents nor for losses in transit, and each correspondent so selected shall not be liable except for its own negligence. This bank or its correspondents may send items directly or indirectly to any bank including the payor, and accept its draft or credit as conditional payment in lieu of cash; it may charge back any item at any time before final payment, whether returned or not, also any item drawn on this bank not good at close of business on day deposited.
All city checks deposited today will be held at depositor's risk until next day's settlement.

Illustration No. 12, Credit Advice

during the month, (c) the amounts of checks honored during the month, (d) other items charged to the depositor's account during the month, and (e) the balance on deposit at the end of the month. With his monthly bank statement, the depositor also receives all checks honored by the bank during the month, together with any other vouchers representing items charged to his account.

Reconciling the Bank Balance. When a bank statement is received, a depositor should check it immediately with the bank record kept on his check stubs. This procedure is known as *reconciling the bank balance.* The balance shown on the bank statement may not be the same as the amount shown on the check stubs for one or more of the following reasons:

STATEMENT OF YOUR ACCOUNT WITH
LIBERTY NATIONAL BANK
REPORT PROMPTLY ANY CHANGE IN YOUR ADDRESS

W. L. Mann
12 N. Third St.
City

CHECKS			DEPOSITS		THE LAST AMOUNT IN THIS COLUMN IS YOUR BALANCE
			BALANCE FORWARD	Sept. 1	8,937.46
50.00	20.96	85.00		2	8,781.50
			600.02	4	9,381.52
641.37	100.00			8	8,640.15
125.00	10.00		349.65	12	8,854.80
321.60	129.75	15.00		15	8,388.45
25.00	152.50		721.30	19	8,932.25
600.00	39.75	5.00		22	8,287.50
125.60				26	8,161.90
17.65	42.50	98.75	591.63	30	8,594.63

VOUCHERS RETURNED 19
SHEET NUMBER 285

Illustration No. 13, Bank Statement

(a) Some of the checks issued during the month may not have been presented to the bank for payment before the statement was prepared.

(b) Deposits made by mail may have been in transit.

(c) Service charges or other charges may appear on the bank statement that the depositor has not recorded on his check stubs.

(d) The depositor may have erred in keeping his bank record.

(e) The bank may have erred in keeping its account with the depositor.

If a depositor is unable to reconcile his bank balance, he should report the matter to his bank immediately.

Following is a suggested procedure in reconciling the bank balance:

(a) The amount of each deposit recorded on the bank statement should be checked with the amount recorded on the check stubs.

(b) The amount of each canceled check should be compared both with the amount recorded on the bank statement and with the amount recorded on the depositor's check stubs. When making this comparison it is a good plan to check the amount recorded on each check stub to indicate that the canceled check has been returned by the bank.

(c) The amounts of any items listed on a bank statement that represent charges to a depositor's account which have not been entered on the check stubs should be deducted from the balance on the check stubs and should be recorded in the cashbook.

(d) A list of the outstanding checks should be prepared. The information needed in preparing this list may be obtained from the check stubs.

After completing the foregoing steps, the balance shown on the check stubs should equal the balance shown in the bank statement less the total amount of the checks outstanding. A common error on the part of depositors is failure to record the amount of *counter checks* issued. Banks usually provide counter checks for the convenience of their depositors in withdrawing funds for personal use. Such checks are canceled and returned to the depositor with the bank statement so that it is an easy matter for the depositor to detect if he has failed to record such checks.

Following is a reconciliation of the bank balance shown in the statement reproduced in Illustration No. 13. In making this reconciliation it was assumed that the depositor's check stub indicated a balance of $8,339.58 on September 30 and that Checks Nos. 112, 115, and 117 had not been presented for payment and thus were not returned with the bank statement.

Bank Balance, September 30, per Statement		$8,594.63
Less Checks Outstanding:		
No. 112	$ 75.00	
No. 115	19.50	
No. 117	160.55	255.05
Check-stub Balance, September 30		$8,339.58

Service Charges. A service charge may be made by a bank for the handling of checks and other items. The basis and the amount of such charges vary with different banks in different localities.

When a bank statement indicates that a service charge has been made, the depositor should record the amount of the service charge by debiting an account with Bank Service Charges and by crediting the bank checking account. He should also deduct the amount of such charges from the check-stub balance before reconciling the bank balance. When a service charge is made, a notice or account analysis usually accompanies the bank statement.

Keeping a Ledger Account with the Bank. As explained previously, a memorandum account with the bank may be kept on the depositor's checkbook stub. The depositor may also keep a ledger account with the bank if desired. The title of such an account should include the name of the bank, followed by the word "Checking." Thus, if a checking account is kept with the Liberty National Bank, the proper title of the ledger account is as shown in the "T" account at the right.

Liberty Nat'l Bank — Checking	

The bank checking account should be debited for the amount of each deposit and should be credited for the amount of each check written. The account should also be credited for any other items that may be charged to the account by the bank, including service charges.

When both a cash account and a bank checking account are kept in the ledger, the following procedure should be observed in recording transactions affecting these accounts:

Cash	
Debit: For all receipts of cash and cash items.	Credit: (a) For all payments in cash. (b) For all bank deposits.

Liberty Nat'l Bank — Checking	
Debit: For all deposits.	Credit: (a) For all checks written. (b) For all service charges. (c) For all other charges, such as for dishonored checks.

Under this method of accounting for cash and banking transactions, the cash account will be in balance when all cash on hand has been deposited in the bank. To prove the balance of the cash account at any time, it is necessary only to count the cash on hand and to compare it with the cash account balance. To prove the bank checking account balance, it will be necessary to reconcile the bank balance in the same manner in which it is reconciled when only a memorandum record of bank transactions is kept on the check stubs.

The cash account can be dispensed with when a bank checking account is kept in the ledger and all cash receipts are deposited in the bank. When this is done, it is advisable to make all disbursements by bank check (except that small expenditures may be made from a petty cash fund as is explained later).

Under this method of accounting, the Cash Receipts Dr. and the Cash Payments Cr. columns of the combined cash-journal may be headed as follows:

	BANK	
	DEPOSITS DR.	CHECKS CR.
1		
2		
3		
4		
5		

When this form of combined cash-journal is used, all cash receipts should be entered in the Bank Deposits Dr. column and all checks issued should be entered in the Bank Checks Cr. column. Daily, or at frequent intervals, the receipts are deposited in the bank. If all cash received during the month has been deposited before the books are closed at the end of the month, the total bank deposits will equal the total cash receipts for the month. If all disbursements during the month are made by check, the total checks issued will equal the total disbursements for the month.

Savings Account. When a savings account is opened in a bank, a signature card must be signed by the depositor. He is then given a passbook that he must present at the bank when making deposits or when making withdrawals. By signing the signature card, the depositor agrees to abide by the rules and the regulations of the bank. These rules and regulations vary with different banks and may be altered and amended from time to time. The principal differences between a savings account and a checking account are that interest is paid by the bank on the former and withdrawals from a savings account must be made at the bank by the depositor or his authorized agent. Interest usually is computed on a semiannual basis. The passbook must be presented along with a withdrawal slip when money is drawn from the account. Banks do not as a rule pay interest on the balances in checking accounts. Depositors use checking accounts primarily as a convenient means of making payments while savings accounts are used primarily as a means of accumulating funds with interest.

When a depositor opens a savings account in a bank, a separate account for it should be set up in his ledger. The proper title for a savings account is the name of the bank, followed by the word "Savings." Thus, if a savings account is kept with the Liberty National Bank, the proper title of the ledger account is as shown in the "T" account at the right. Under no circumstances should a savings account be confused with a checking account. It should always be a separate account and, as such, it should be debited for each deposit and should be credited for each withdrawal. Semiannually, or at such times as interest is credited to the account by the bank, entries should be made in the books of the depositor debiting the bank savings account and crediting Interest Income.

LIBERTY NATIONAL BANK — SAVINGS

The amount of interest credited to a depositor's savings account by a bank should be recorded in the books of the depositor as income whether or not the interest is withdrawn in cash. Interest on a savings account is taxable income to the depositor in the year in which it is credited to his account, even though he keeps his books on the cash basis and does not withdraw the interest in cash during the year.

PRACTICE ASSIGNMENT No. 9. Complete Report No. 9 in the workbook and submit your working papers to the instructor for approval. After completing the report, continue with the following study assignment until Report No. 10 is required.

X THE PETTY CASH FUND

It is a good business policy to deposit in a bank all cash received. When this is done, the total cash receipts and the total bank deposits will be equal. It is also a good policy to make arrangements with the bank so that all checks and other cash items received from customers or others in the usual course of business will be accepted for deposit only. Arrangements may also be made with the bank so that no item will be charged to the depositor's account until a check from the depositor for the proper amount is obtained. For example, the bank will by arrangement present dishonored checks to the depositor for payment, instead of charging them to the depositor's account. Service charges too may be paid by check.

When all cash and cash items received are deposited in a bank, an office fund or petty cash fund may be established for paying small items. Such a petty cash fund eliminates the necessity of writing checks for small amounts to pay miscellaneous bills.

Establishing a Petty Cash Fund. To establish a *petty cash fund,* a check should be drawn for the amount that is to be set aside in the fund. The amount may be $25, $50, $100, or any amount considered necessary. The check is usually made payable to "Cash," "Petty Cash," or "Office Fund." When the check is cashed by the bank, the money is placed in a cash drawer, a cash register, or a safe at the depositor's place of business, and a designated individual in the office is authorized to make payments from the fund. The one who is responsible for the fund should be able to account for the amount of the fund at any time. Disbursements from the fund should not be made without a voucher or a receipt. A form of petty cash voucher is shown in Illustration No. 14. Such a voucher should be used for all expenditures for which no invoice has been received.

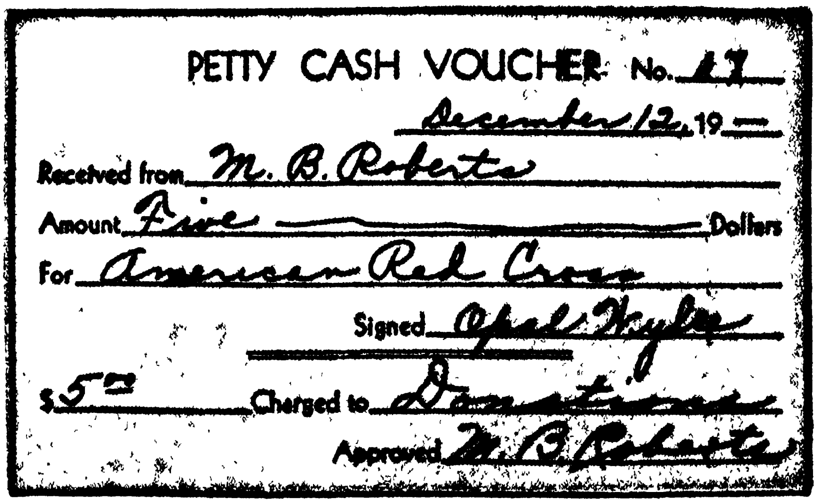


Illustration No. 14, Petty Cash Voucher

The only entry required to record the check drawn to establish the petty cash fund is an entry in the combined cash-journal debiting Petty Cash Fund and crediting the bank checking account. When it is necessary to replenish the fund, the petty cashier usually prepares a statement of the expenditures properly classified. A check is then drawn for the exact amount of the total expenditures. This check is recorded in the combined cash-journal by debiting the respective expense accounts indicated in the statement and by crediting the bank checking account.

The petty cash fund represents a revolving fund that does not change in amount unless the fund is increased or decreased. The actual amount of cash in the fund plus the total of the petty cash vouchers or receipts should always be equal to the amount originally charged to the petty cash fund.

Petty Cash Disbursements Record. When a petty cash fund is maintained, a record should be kept of all disbursements from the fund. Various types of records have been designed for this purpose. One of the standard forms is illustrated on page 119. The headings of the Distribution columns may vary with each enterprise depending upon the desired classification of petty expenditures. It should be remembered that the headings represent accounts that are to be charged for the expenditures. The desired headings may either be printed on the form or may be written in by hand. Sometimes numbers instead of account titles are used in the headings to represent the accounts to be charged.

The petty cashier should have a voucher for each disbursement made from the petty cash fund. Unless an invoice or receipt is obtained that will serve as a voucher, the petty cashier should provide the necessary voucher. The vouchers should be numbered consecutively.

A narrative of the petty cash transactions completed by M. B. Roberts' secretary during the month of December appears on page 118. Since he is out of the office much of the time, he considers it advisable to provide a petty cash fund from which his secretary is authorized to make miscellaneous disbursements not to exceed $5 each.

Proving the Petty Cash Disbursements Record. To prove the petty cash disbursements record, it is first necessary to foot all of the amount columns. The sum of the footings of the Distribution columns should equal the footing of the Total Amount column. After proving the footings, the totals should be recorded and the record should be ruled as shown in the illustration. The illustration shows that a total of a $43.60 was paid out during December. Since it was desired to replenish the petty cash fund at this time, the following statement of the disbursements for December was prepared:

STATEMENT OF PETTY CASH DISBURSEMENTS
FOR DECEMBER

Telephone and Telegraph Expense	$ 1.25
Automobile Expense	4.00
Stationery and Supplies	9.10
Donations	6.50
Advertising	4.00
Traveling Expense	3.75
Miscellaneous Expenses	10.00
M. B. Roberts, Drawing	5.00
Total Disbursements	$43.60

The statement of expenditures serves as a voucher authorizing the issuance of a check for $43.60 to replenish the petty cash fund. After footing and ruling the petty cash disbursements record, the balance in the fund and the amount received to replenish the fund may be recorded in the Description column below the ruling as shown in the illustration. It is customary to carry the total amount in the fund forward to the top of a new page before recording any of the transactions for the ensuing month.

The petty cash disbursements record reproduced on page 119 is an auxiliary record that supplements the regular accounting records. No posting is required from this auxiliary record. The total amount of the expenditures from the petty cash fund is entered in the combined cash-journal at the time of replenishing the fund by debiting the proper expense accounts and by crediting the bank checking account. The statement of petty cash disbursements provides the information needed in recording the check issued to replenish the petty cash fund. The required posting is done from the combined cash-journal.

The method of recording the check issued by M. B. Roberts on December 1 to create a petty cash fund and the check issued on December 30 to replenish the fund is illustrated on page 120. It is assumed that Mr. Roberts used a combined cash-journal ruled like the one illustrated on page 120. However, the last four amount columns are omitted from the illustration since they are not used in recording these transactions.

NARRATIVE OF PETTY CASH TRANSACTIONS

M. B. Roberts, Proprietor

Dec. 1. (Friday) Issued check for $50 payable to Petty Cash, cashed the check, and placed the proceeds in a petty cash fund.

This transaction was recorded in the combined cash-journal by debiting Petty Cash Fund and by crediting the bank checking account. A memorandum entry was also made in the Description column of the petty cash disbursements record reproduced on page 119.

During the month of December the following disbursements were made from the petty cash fund:

2. Paid $2 for washing windows. Voucher No. 1.
5. Gave Mr. Roberts $3 to reimburse him for the amount spent in having his automobile repaired. Voucher No. 2.
7. Gave Mr. Roberts $3 to reimburse him for the amount spent in entertaining client at luncheon. Voucher No. 3.
8. Paid $1 for messenger fees. Voucher No. 4.
9. Paid $4 for an announcement in local newspaper. Voucher No. 5.
11. Gave Mr. Roberts $5 for personal use. Voucher No. 6.

This item was entered in the Amount column provided at the extreme right of the petty cash disbursements record since no special distribution column had been provided for recording amounts withdrawn by the proprietor for personal use.

12. Gave the Red Cross a $5 donation. Voucher No. 7.
14. Paid 50 cents for typewriter repairs. Voucher No. 8.
16. Gave Mr. Roberts $3.75 to reimburse him for traveling expenses. Voucher No. 9.
18. Gave Mr. Roberts $1 to reimburse him for the amount spent in having his automobile washed. Voucher No. 10.
20. Paid $3.50 for cleaning office. Voucher No. 11
22. Paid $1.25 for collect telegram. Voucher No. 12.
23. Gave the Salvation Army a donation of $1.50. Voucher No. 13.
26. Paid $2.40 for office supplies, including blotters, ink, and pencils. Voucher No. 14.
28. Paid $4.70 for letterheads and envelopes. Voucher No. 15.
30. Paid $2 for office supplies. Voucher No. 16.
30. Issued check for $43.60 to replenish the petty cash fund.

PETTY CASH DISBURSEMENTS FOR MONTH OF December 19–

DAY	DESCRIPTION	VOU. NO.	TOTAL AMOUNT	DISTRIBUTION OF CHARGES: T.&T.	Auto Ex.	S.&S.	Don.	Adv.	Trav. Ex.	Misc. Ex.		ACCOUNT	AMOUNT
	BROUGHT FORWARD												
1	Received in fund $50	✓											
2	Washing windows	1	2 00							2 00			
5	Auto repairs	2	3 00		3 00								
7	Client at luncheon	3	3 00							3 00			
8	Messenger	4	1 00							1 00			
9	Advertising	5	4 00					4 00					
11	Mr. Roberts, Personal	6	5 00									M. B. Roberts, Draw.	5 00
12	Red Cross	7	5 00				5 00						
14	Type. repairs	8	50							50			
16	Traveling expenses	9	3 75						3 75				
18	Washing auto	10	1 00		1 00								
20	Cleaning office	11	3 50							3 50			
22	Collect telegram	12	1 25	1 25									
23	Salvation Army	13	1 50				1 50						
26	Office supplies	14	2 40			2 40							
28	Letterheads & envelopes	15	4 70			4 70							
30	Office supplies	16	2 00			2 00							
			43 60	1 25	4 00	9 10	6 50	4 00	3 75	10 00			5 00
30	Balance $6.40												
30	Rec'd in fund 43.60												
	Total $50.00												

Petty Cash Disbursements Record

M. B. ROBERTS' COMBINED CASH-JOURNAL

Bank Deposits Dr.	Bank Checks Cr.	Date Mo.	Date Day	Description	Post. Ref.	General Debits	General Credits
				Amounts Forwarded			
	50.00	Dec.	1	Petty Cash Fund		50.00	
	43.60		30	Tel. & Tel. Expense		1.25	
				Auto. Expense		4.00	
				Stationery & Supplies		9.10	
				Donations		6.50	
				Advertising		4.00	
				Traveling Expenses		3.75	
				Misc. Expenses		10.00	
				M. B. Roberts, Drawing		5.00	

The foregoing method of handling a petty cash fund is sometimes referred to as the *imprest method*. It is the method most commonly used. In some cases, however, a petty cash disbursements record is used as a journal, in which case it serves as a posting medium. If the disbursements are posted direct from the petty cash disbursements record to the proper accounts, the check drawn to replenish the fund is recorded in the combined cash-journal by debiting Petty Cash Fund and by crediting the bank checking account. A check mark is then placed in the Posting Reference column to indicate that the entry should not be posted to the debit of Petty Cash Fund. The credit to the bank checking account in the combined cash-journal is offset by the debits posted from the petty cash disbursements record.

***PRACTICE ASSIGNMENT No. 10.** Refer to the workbook and complete Report No. 10. This practice assignment provides a test of your ability to apply the principles developed in the first four units of the textbook. After completing the report, you may proceed with the textbook discussion in Unit Five until the next report is required.*

Unit Five

ACCOUNTING FOR NOTES AND SECURITIES

XI NOTES AND INTEREST

The owner of an enterprise may acquire or issue notes in the usual course of business. Notes received constitute an asset that is usually classified as notes receivable. Notes issued constitute a liability that is usually classified as notes payable. Notes receivable and notes payable may be either interest bearing or noninterest bearing.

Notes Receivable. A note is an unconditional promise in writing to pay a specified sum of money to order or to bearer at a stated or determinable future time. A note that conforms to all of the requirements established by law so that it may be transferred freely in the ordinary course of business is a *negotiable note.* An analysis of the note reproduced in Illustration No. 15 reveals that it possesses the following essentials of negotiability:

(a) It is in writing. The fact that it is partly printed and partly written is immaterial.

(b) It is signed by the party executing it — *James Marsh.*

(c) It contains a promise to pay.

(d) The promise is unconditional.

(e) It provides for the payment of a sum certain in money—*$286.50.* The amount is specified in both figures and words, which is the usual custom.

(f) It is payable at a determinable future time—*July 5, 19—.*

(g) It is payable to the order of *Robert Clarkson,* the payee.

In addition to the foregoing essentials of negotiability, the note illustrated also specifies the following:

(a) Date of issue — *April 6, 19—.*

(b) Place of payment — *State Bank, Macon.* The place of payment need not be specified.

(c) Rate of interest — *6%.* A negotiable note may be interest bearing or noninterest bearing.

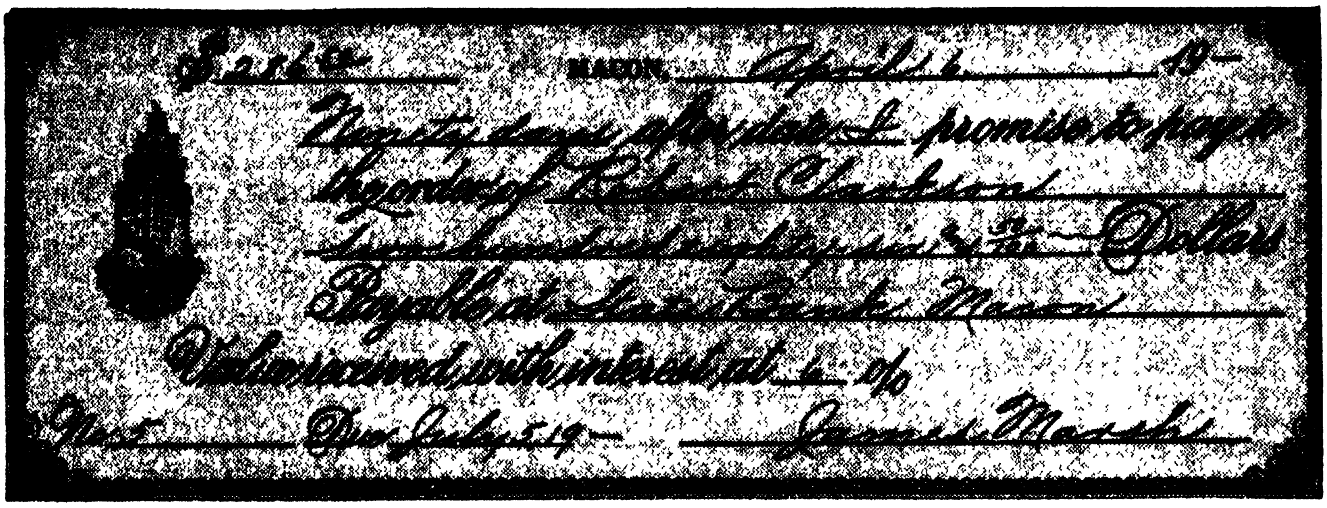


Illustration No. 15, Interest-Bearing Negotiable Note

Notes Receivable Account. When merchandise is sold to a customer on credit, the transaction is recorded by debiting Accounts Receivable and by crediting Sales. Should the customer desire to obtain an extension of time for the payment of the debt, he may issue a note for thirty, sixty, or ninety days, or for some other period of time. When a note is accepted from a customer in temporary settlement of his account, the note should be recorded by debiting Notes Receivable and by crediting Accounts Receivable. The notes receivable account should be debited for the face amount of each note received and should be credited for the face amount of each note paid by the maker.

Interest Income Account. When an interest-bearing note is owned, the interest on it may be received periodically or upon maturity of the note. In the case of short-term notes, the interest is usually payable at maturity of the note. In the case of long-term notes, the interest may be payable semiannually or annually. Interest may be received also on bank deposits, bonds, mortgages, and other interest-bearing obligations owned. When interest is received, it should be recorded by debiting Cash and by crediting Interest Income.

Application of Principles. The following selected transactions were completed by R. W. Hill, a retail merchant. These transactions are first recorded in general journal form and are then posted to the proper general ledger accounts. (See page 124)

NARRATIVE OF TRANSACTIONS

October 16. Sold M. D. Wright merchandise on 30 days credit, $350.
November 1. Sold R. R. Philips merchandise on 30 days credit, $400.

November 15. Received from M. D. Wright a check for $50 to apply on his account and a 30-day, 6% note for $300 in temporary settlement of the balance. Mr. Hill agrees to accept the note.

December 1. In order to obtain an extension of time on his account, R. R. Philips submits a 60-day, 6% note for $400, which Mr. Hill accepts.

December 15. Received a check for $301.50 from M. D. Wright in payment of the principal and interest on his note due today.

Analysis of Transactions. The transactions of October 16 and November 1 resulted in increases in the asset accounts receivable with corresponding increases in sales income; hence both transactions were recorded by debiting Accounts Receivable and by crediting Sales.

The transaction of November 15 resulted in an increase in cash amounting to $50, an increase in notes receivable amounting to $300, and a decrease in accounts receivable amounting to $350; hence it was recorded by debiting Cash for $50 and Notes Receivable for $300 and by crediting Accounts Receivable for $350.

The transaction of December 1 resulted in an increase in the asset notes receivable with a corresponding decrease in the asset accounts receivable; hence it was recorded by debiting Notes Receivable and by crediting Accounts Receivable.

The transaction of December 15 resulted in an increase in cash amounting to $301.50, a decrease in notes receivable amounting to $300, and an increase in interest income amounting to $1.50; hence it was recorded by debiting Cash for $301.50 and by crediting Notes Receivable for $300 and Interest Income for $1.50.

Notes Payable. Notes may be issued for the following purposes:

(a) To obtain a loan from a bank or other source.
(b) In exchange for property purchased.
(c) To obtain an extension of time on an account payable.

Notes issued for such purposes are usually interest bearing and generally are issued for a relatively short period of time, such as thirty, sixty, or ninety days.

Notes Payable Account. It is customary to keep separate accounts for accounts payable and for notes payable, even though the creditor is the same party. When merchandise or other property is purchased on credit, the transaction is recorded by debiting Purchases or the proper asset account and by crediting Accounts Payable. Should an extension of time on the account be desired, the creditor may request an interest-

General Journal

*Oct. 16.	Accounts Receivable	$350.00	
	Sales		$350.00
	M. D. Wright — 30 days.		
Nov. 1.	Accounts Receivable	400.00	
	Sales		400.00
	R. R. Philips — 30 days.		
15.	Cash	50.00	
	Notes Receivable	300.00	
	Accounts Receivable		350.00
	Received check for $50 and a 30-day, 6% note for $300 from M. D. Wright.		
Dec. 1.	Notes Receivable	400.00	
	Accounts Receivable		400.00
	Received 60-day, 6% note from R. R. Philips.		
15.	Cash	301.50	
	Notes Receivable		300.00
	Interest Income		1.50
	Received check in payment of M. D. Wright's note — principal $300, interest $1.50.		

General Ledger

Cash

Nov. 15	50.00		
Dec. 15	301.50		

Sales

		Oct. 16	350.00
		Nov. 1	400.00

Notes Receivable

Nov. 15	300.00	Dec. 15	300.00
Dec. 1	400.00		

Interest Income

		Dec. 15	1.50

Accounts Receivable

Oct. 16	350.00	Nov. 15	350.00
Nov. 1	400.00	Dec. 1	400.00

*These journal entries are arranged in skeleton form. The position of the account titles and amounts indicates whether they are debits or credits. It will be noted that debit items are written to the left and credit items to the right.

bearing note. When a note is issued to a creditor in temporary settlement of an account, it should be recorded by debiting Accounts Payable and by crediting Notes Payable. The notes payable account should be credited for the face amount of each note issued and should be debited for the face amount of each note paid.

Interest Expense Account. Interest may be paid on notes, bonds, mortgages, and other interest-bearing obligations outstanding. When interest is paid, it should be recorded by debiting Interest Expense and by crediting Cash.

Application of Principles. The following selected transactions were completed by R. W. Hill, a retail merchant. These transactions are first recorded in general journal form and are then posted to the proper general ledger accounts. (See page 126)

NARRATIVE OF TRANSACTIONS

September 15. Purchased merchandise from the Campbell Furniture Co., $600. Terms, 2/30, n/60.

October 1. Purchased merchandise from Brown Bros., $300. Terms, net 30 days.

November 1. In order to obtain an extension of time on the account of Brown Bros., a 30-day, 6% note for $300 was tendered and accepted.

November 11. Borrowed $500 from the Liberty National Bank giving the bank a 60-day, 5% note.

November 15. Issued a check for $200 to the Campbell Furniture Co. to apply on account and gave them a 60-day, 5% note for $400 in temporary settlement of the balance.

December 1. Issued a check for $301.50 to Brown Bros. in payment of the principal and interest on note due today.

December 11. Purchased a new desk from the Office Supply Co. paying $50 in cash and giving a 30-day, 6% note for $100.

Analysis of Transactions. The transactions of September 15 and October 1 resulted in increases in purchases with corresponding increases in the liability accounts payable; hence both transactions were recorded by debiting Purchases and by crediting Accounts Payable.

The transaction of November 1 resulted in a decrease in the liability accounts payable with a corresponding increase in the liability notes payable; hence it was recorded by debiting Accounts Payable and by crediting Notes Payable.

General Journal

Sept. 15.	Purchases	$600.00	
	Accounts Payable		$600.00
	Campbell Furniture Co. — 2/30, n/60.		
Oct. 1.	Purchases	300.00	
	Accounts Payable		300.00
	Brown Bros. — net, 30 days.		
Nov. 1.	Accounts Payable	300.00	
	Notes Payable		300.00
	Gave Brown Bros. 30-day, 6% note.		
11.	Cash	500.00	
	Notes Payable		500.00
	Borrowed $500 from the Liberty National Bank on 60-day, 5% note.		
15.	Accounts Payable	600.00	
	Cash		200.00
	Notes Payable		400.00
	Gave Campbell Furniture Co. check for $200 and 60-day, 5% note for $400.		
Dec. 1.	Notes Payable	300.00	
	Interest Expense	1.50	
	Cash		301.50
	Gave Brown Bros. check in payment of note — principal $300, interest $1.50.		
11.	Office Equipment	150.00	
	Cash		50.00
	Notes Payable		100.00
	Gave the Office Supply Co. check for $50 and 30-day, 6% note for $100 in payment of office desk.		

General Ledger

Cash

Nov. 11	500.00	Nov. 15	200.00
		Dec. 1	301.50
		11	50.00

Accounts Payable

Nov. 1	300.00	Sept. 15	600.00
15	600.00	Oct. 1	300.00

Office Equipment

Dec. 11	150.00		

Purchases

Sept. 15	600.00		
Oct. 1	300.00		

Notes Payable

Dec. 1	300.00	Nov. 1	300.00
		11	500.00
		15	400.00
		Dec. 11	100.00

Interest Expense

Dec. 1	1.50		

The transaction of November 11 resulted in an increase in the asset cash with a corresponding increase in the liability notes payable; hence it was recorded by debiting Cash and by crediting Notes Payable.

The transaction of November 15 resulted in a decrease in accounts payable amounting to $600, an increase in notes payable amounting to $400, and a decrease in cash amounting to $200; hence it was recorded by debiting Accounts Payable for $600 and by crediting Cash for $200 and Notes Payable for $400.

The transaction of December 1 resulted in a decrease in notes payable amounting to $300, an increase in interest expense amounting to $1.50, and a decrease in cash amounting to $301.50; hence it was recorded by debiting Notes Payable for $300 and Interest Expense for $1.50 and by crediting Cash for $301.50.

The transaction of December 11 resulted in an increase in office equipment amounting to $150, a decrease in cash amounting to $50, and an increase in notes payable amounting to $100; hence it was recorded by debiting Office Equipment for $150 and by crediting Cash for $50 and Notes Payable for $100.

PRACTICE ASSIGNMENT No. 11. Complete Report No. 11 in the workbook and submit your working papers to the instructor for approval. After completing the report, continue with the following study assignment until the next report is required.

XII SECURITIES

Securities purchased for investment purposes may include bonds and stocks. Income may be derived from the interest received on bonds or from the dividends received on stocks. The following is a brief outline of the principles involved in recording the purchase of securities:

(a) Securities purchased for cash should be recorded by debiting the proper asset account and by crediting Cash for the amount paid for the securities.

(b) Securities purchased on credit should be recorded by debiting the proper asset account and by crediting Accounts Payable for the purchase price.

(c) Securities purchased on terms involving part payment in cash and the balance on credit should be recorded by debiting the proper asset account for the purchase price, and by crediting Cash for the amount paid and crediting Accounts Payable for the balance.

(d) Securities purchased on terms involving part payment in cash and a note for the balance should be recorded by debiting the proper asset account for the purchase price, and by crediting Cash for the amount paid and crediting Notes Payable for the amount of the note issued.

Summarizing the foregoing discussion, the following general rule may be established as a guide in recording the purchase of securities:

Debit the proper account for the purchase price of the security, and
Credit: (a) Cash for the amount paid, and
(b) The proper liability account for the balance, if any.

Bonds. For the purpose of this discussion, bonds are divided into two general classes: namely, government bonds and corporation bonds. Government bonds include obligations of the United States, such as Postal Savings Bonds, U. S. Savings Bonds, and U. S. Treasury Bonds. Bonds guaranteed by the United States, such as the Home Owners' Loan Corporation Bonds and the Federal Farm Mortgage Corporation Bonds, are generally classified as government bonds also. State bonds are obligations of the respective states. Municipal bonds are obligations of the respective municipalities. Bonds are issued by other subdivisions of the states also, including school districts, conservancy districts, counties, and townships. All such bonds are considered government bonds.

Private corporations may issue bonds as a means of borrowing money. Corporation bonds may be secured by a mortgage on specific assets of the corporation. Many different types of corporation bonds are issued. It is not the purpose here to enter into a discussion of all these types of bonds but rather to differentiate between government bonds and private corporation bonds. The accounting procedure in recording bonds purchased for investment purposes is the same with all types of bonds. To illustrate the accounting procedure in recording bonds purchased as an investment and held for income purposes, U. S. Savings Bonds, U. S. Treasury Bonds, and corporation bonds will be considered.

U. S. Savings Bonds. Since 1935 the Federal Government has been issuing savings bonds. These bonds are of two general types. The non-interest-bearing bonds that are issued at a discount and are redeemable, at the option of the owner, at increasing fixed values are known as *appreciation bonds.* The interest-bearing bonds that are issued at par value and are redeemable, at the option of the owner, at fixed redemption values are known as *current income bonds.* Currently Series E, F, and G Bonds are being issued. The Series E and F Bonds are appreciation bonds; the G Bonds are current income bonds.

Series E Bonds. Series E Bonds have been issued since 1941 in denominations (maturity value) of $25 to $1,000. The issue price is 75 per cent of the maturity value. The bonds are dated the first day of the month in which payment is received by an authorized issuing agent. The bonds are due ten years from issue date and, when held to maturity, yield about 2.9 per cent compounded semiannually. At the option of the owner, they may be redeemed at any time after 60 days from issue date. Redemption values are shown in the table on page 131.

Series F Bonds. Series F Bonds have been issued since 1941 in denominations (maturity value) of $25 to $10,000. The issue price is 74 per cent of the maturity value. The bonds are dated the first day of the month in which payment is received by a Federal Reserve Bank or branch of the Treasury. The bonds are due twelve years from issue date and, when held to maturity, yield about 2.53 per cent compounded semiannually. At the option of the owner, they may be redeemed after six months from issue date. Redemption values are shown in the table on page 131.

Series G Bonds. Series G Bonds have been issued since 1941 in denominations of $100 to $10,000. The issue price is 100 per cent of the maturity value. The bonds are dated the first day of the month in which payment is received by a Federal Reserve Bank or branch of the Treasury. The bonds are due twelve years from issue date and, when held to maturity, yield 2.5 per cent. The interest is payable semiannually by Treasury check. Redemption values are shown in the table on page 131.

The purchase of U. S. Savings Bonds of the Series E and F type should be recorded by debiting Government Bonds and by crediting Cash for the cost price. Thus, if a $1,000 Series E bond is purchased at the issue price of $750, the transaction should be recorded as indicated in the following general journal entry:

Government Bonds..................................	$750.00	
Cash..		$750.00
Purchased a $1,000 U. S. Savings Bond, Series E.		

The appreciation or increase in the value of Series E and F Bonds may, at the option of the owner, be treated either as current income or deferred income for income tax purposes. If the purchaser of Series E and F Bonds elects to treat the appreciation as current income, an entry should be made each year to record the amount of the increased value or increment resulting from the accumulation of interest. By referring to the redemption table on page 131 it will be noted that there is no increase in the value of a Series E Bond the first year, but at the end of the second year its redemption value is $760, an increase of $10 above cost. This increase in the value of the bond should be recorded as indicated in the following general journal entry:

Government Bonds	$10.00	
Interest Income		$10.00
Increased redemption value of a $1,000 U. S. Savings Bond, Series E.		

Upon maturity, when all appreciation has been recorded, the total debits to the bond account should equal the maturity value of the bond. When the bond is redeemed, the transaction should be recorded by debiting Cash and by crediting Government Bonds for $1,000.

If the purchaser of a $1,000 Series E Bond for $750 prefers to treat the appreciation as deferred income, the appreciation need not be recorded until the bond is redeemed. If the bond is redeemed at maturity, the transaction should be recorded as indicated in the following general journal entry:

Cash	$1,000.00	
Government Bonds		$750.00
Interest Income		250.00
Redeemed a $1,000 U. S. Savings Bond, Series E.		

Treating the appreciation in Series E and F Bonds as current income is advantageous taxwise to many buyers because it results in a more uniform distribution of the income over the life of the bond instead of treating the entire amount as income in the year in which the bond is redeemed.

Since U. S. Savings Bonds of the Series G type are not issued at a discount, they cannot be purchased for less than their face value. Thus, when a $1,000 Series G bond is purchased, the transaction should be recorded by debiting Government Bonds and by crediting Cash for $1,000. The interest on these bonds is paid semiannually by U. S. Treasury checks, which are mailed direct to the registered owner. When such checks are received, they should be recorded by debiting Cash and by crediting Interest Income.

U. S. Treasury Bonds. U. S. Treasury Bonds may be subscribed for at the time of original issue or they may be purchased subsequently at the prevailing market price through banks and brokerage houses or from private holders. The accounting procedure in recording the purchase of these bonds differs only slightly from the procedure in recording U. S. Savings Bonds that are purchased at a discount. The face value of U. S. Treasury Bonds is constant, and the government pays the interest on the

REDEMPTION VALUES OF UNITED STATES SAVINGS BONDS

(Per $100.00 of Maturity Value)

Period after issue date	Series E Savings Bonds	Series F Savings Bonds	Series G Savings Bonds
First ½ year	$75.00	Not redeemable	Not redeemable
½ to 1 year	75.00	$74.00	$98.80
1 to 1½ years	75.50	74.20	97.80
1½ to 2 years	76.00	74.50	96.90
2 to 2½ years	76.50	74.90	96.20
2½ to 3 years	77.00	75.40	95.60
3 to 3½ years	78.00	76.00	95.10
3½ to 4 years	79.00	76.70	94.80
4 to 4½ years	80.00	77.60	94.70
4½ to 5 years	81.00	78.60	94.70
5 to 5½ years	82.00	79.70	94.90
5½ to 6 years	83.00	80.90	95.20
6 to 6½ years	84.00	82.20	95.50
6½ to 7 years	86.00	83.50	95.80
7 to 7½ years	88.00	84.80	96.10
7½ to 8 years	90.00	86.10	96.40
8 to 8½ years	92.00	87.40	96.70
8½ to 9 years	94.00	88.70	97.00
9 to 9½ years	96.00	90.00	97.30
9½ to 10 years	98.00	91.40	97.60
10 to 10½ years		92.90	97.90
10½ to 11 years		94.50	98.20
11 to 11½ years		96.20	98.60
11½ to 12 years		98.00	99.20
MATURITY VALUE*	100.00	100.00	100.00

*Available ten years after issue date for the Series E Savings Bonds and twelve years after issue date for the Series F and G Savings Bonds.

bonds at a fixed rate. The interest is payable semiannually. The bonds are issued in various denominations.

When U. S. Treasury Bonds are subscribed for and obtained at the original issue price, they should be recorded by debiting Government Bonds and by crediting Cash for the cost of the bonds. The cost will be the par value of the bonds, that is, the value specified on the face of the bonds.

When U. S. Treasury Bonds are purchased subsequent to date of issue, the transaction should be recorded similarly, that is, by debiting Government Bonds and by crediting Cash for the cost of the bonds. Because of market conditions, the cost may be more or less than the par value of the bonds. The quoted market prices of U. S. Treasury Bonds do not include either commission charges or accrued interest.

When the bonds are purchased through a bank or a brokerage firm, it will be necessary for the purchaser to pay a commission. The commission represents a part of the cost of the bonds and should be so recorded. If an individual purchases a U. S. Treasury 2½%, $1,000 Bond, to mature in 1965, at a total cost of $1,081.60, including the bank's or the broker's commission, the transaction should be recorded as indicated in the following general journal entry:

Government Bonds	$1,081.60	
Cash		$1,081.60
Purchased a $1,000 U. S. Treasury Bond.		

The foregoing entry is based on the assumption that no interest had accrued on the bond at the time of purchase. If interest amounting to $7.53 had accrued, the total cost would be increased proportionately and the transaction should be recorded as indicated in the following general journal entry:

Government Bonds	$1,081.60	
Accrued Interest Receivable	7.53	
Cash		$1,089.13
Purchased a $1,000 U. S. Treasury Bond.		

The amount charged to Accrued Interest Receivable represents the amount paid for the right to receive the interest already accrued on the bond at the time of purchase.

Interest on U. S. Treasury Bonds, which is payable semiannually, should be recorded by debiting Cash and by crediting Interest Income for the amount of the interest received.

When a bond is sold prior to maturity or when it is redeemed upon maturity, the transaction should be recorded by debiting Cash for the proceeds received and by crediting Government Bonds for the cost of the bond. If the amount received for the bond is more than the original cost of the bond, the excess represents a profit that should be recorded by crediting Gain on Government Bonds. If the amount received for the bond is less than the original cost of the bond, the difference represents a loss that should be recorded by debiting Loss on Government Bonds.

If the U. S. Treasury Bond referred to previously as having cost $1,081.60 were sold through a broker and the proceeds amounted to $1,124.50 after deducting the broker's commission, the transaction should be recorded as indicated in the following general journal entry:

Cash	$1,124.50	
Government Bonds		$1,081.60
Gain on Government Bonds		42.90
Sold a $1,000 U. S. Treasury Bond.		

The foregoing entry is based on the assumption that no interest had accrued on the bond at the time of sale. If interest amounting to $9 had accrued at the time of sale, the selling price would be increased proportionately and the transaction should be recorded as indicated in the following general journal entry:

Cash	$1,133.50	
Interest Income		$ 9.00
Government Bonds		1,081.60
Gain on Government Bonds		42.90
Sold a $1,000 U. S. Treasury Bond.		

The additional amount received because of the interest accrued at the time of the sale is recorded as a credit to Interest Income. Any interest accrued prior to the sale of the bond represents earned income that is realized when the bond is sold. It should be understood that the broker's commission is treated as a deduction from the selling price of the bond and that only the net proceeds are recorded. The gain is the difference between the total cost and the net amount received from the sale of the bond less any accrued interest.

Other Government Bonds. Government bonds may include bonds issued by the states or any of their subdivisions such as counties, townships, municipalities, and school districts. Such bonds should be accounted for in the same manner as U. S. Treasury Bonds, that is, all such bonds should be charged to Government Bonds at cost at the time of purchase. When such bonds are sold prior to maturity or are redeemed at maturity, Government Bonds should be credited for the cost and any gain that is realized should be credited to Gain on Government Bonds or any loss sustained should be debited to Loss on Government Bonds.

Corporation Bonds. The purchase of bonds issued by private corporations should be recorded by debiting Corporation Bonds and by crediting Cash for the cost of the bonds. The cost is the purchase price regardless of whether the price paid is more or less than the par value or the face value of the bonds. If the bonds are purchased through a bank or a brokerage firm and a commission is paid, the commission should be treated as a part of the cost of the bonds.

Corporation bonds generally bear interest at a fixed rate payable annually or semiannually. When interest on corporation bonds is received, it should be recorded by debiting Cash and by crediting Interest Income for the amount of the interest received.

When a corporation bond is sold prior to maturity or is redeemed at maturity and the net amount received is greater than the cost, the transaction should be recorded by debiting Cash for the net amount received and by crediting (a) Corporation Bonds for the cost of the bonds and (b) Gain on Corporation Bonds for the difference between the cost and the proceeds of the sale.

When a corporation bond is sold prior to maturity or is redeemed at maturity and the net amount received is less than the cost, the transaction should be recorded by debiting (a) Cash for the net amount received and (b) Loss on Corporation Bonds for the difference between the cost and the proceeds of the sale, and by crediting Corporation Bonds for the cost of the bonds.

If the bonds are sold through a bank or a brokerage firm and a commission is paid, the commission should be treated as a deduction from the selling price and the net proceeds only should be recorded.

Example: January 15 — Purchased a 4%, $1,000 Union Terminal Company Bond through a broker and paid a total of $1,072.25, including the broker's commission.

July 15 — Sold the Union Terminal Company Bond purchased on January 15 through a brokerage firm and received a check for the net proceeds amounting to $1,125.18.

The foregoing transactions should be recorded as indicated in the following general journal entries:

Jan. 15.	Corporation Bonds	$1,072.25	
	Cash		$1,072.25
	Purchased a $1,000 Union Terminal Company Bond.		
July 15.	Cash	1,125.18	
	Corporation Bonds		1,072.25
	Gain on Corporation Bonds		52.93
	Sold a $1,000 Union Terminal Company Bond.		

The entries for the transactions of January 15 and July 15 assume that there was no interest accrued on the bond either at the time of the purchase or at the time of the sale. Any interest accrued on the bond at the time of purchase should be recorded by debiting Accrued Interest Receivable. The purchase price would be increased in proportion to the amount of the interest accrued, hence the credit to Cash would be correspondingly increased. Any interest accrued at the time of the sale should be recorded by crediting Interest Income. The selling price would be increased in proportion to the amount of the interest accrued, hence the debit to Cash would be correspondingly increased.

Corporation Stocks. The ownership of a private corporation is evidenced by certificates of stock, commonly known as capital stock. Shares of capital stock may be purchased as an investment. There are two principal classes of capital stock, known as common stock and preferred stock. The *common stock* of a corporation is ordinary stock that has no preference as to principal or dividends. The *preferred stock* of a corporation is capital stock that has some preference as to principal or dividends, or both. The preferred stock may rank ahead of the common stock in the stockholder's right to receive dividends or in his right to receive prior payment for his stock in case of dissolution of the company. In considering the relative merits of common stock and preferred stock, careful consideration should be given to all of the factors involved. While preferred stock is generally considered to be a more conservative investment than common stock, it may not, in a particular case, be a better investment than the common stock of the same company. The mere designation of stock as preferred stock does not necessarily indicate its greater value.

Capital stock, whether common or preferred, may or may not have a designated par value. If capital stock has par value, the value will be stated on the stock certificate; if it has no par value, that fact will be stated on the stock certificate.

If a corporation has the authority to issue 100 shares of common capital stock with par value of $100 per share and all of the stock is sold at its par value, the corporation's capital will amount to $10,000. The owner of each share of stock will actually own 1/100 of the corporation, and the owner of 10 shares of stock will own 1/10 of the corporation.

The par value of capital stock should not be confused with its market value, as these values may differ materially. The par value is the stated value expressed on the stock certificate, while the market value is the price at which the stock may be purchased or sold in the open market. Investors are primarily interested in the market value of the share of capital stock that they may own or may desire to purchase.

Interest is not paid on capital stock. Income from capital stock is derived from dividends received rather than from interest received. In this respect capital stock differs materially from bonds that may be issued by the same corporation. The fact should not be overlooked that the ownership of capital stock represents direct ownership of a portion of the issuing corporation. On the other hand the ownership of bonds puts the bondholder in the position of a creditor who has loaned money to the issuing corporation and who has received in return the promise of the corporation to redeem its bonds at a specified date and to pay in the meantime a specified rate of interest on the bonds.

When capital stock is purchased as an investment, it may be recorded by debiting an investment account entitled Corporation Stocks and by crediting Cash for the amount paid for the stock. If desired, a separate account may be kept for each company's stock purchased. For example, if an investor should purchase common stock of the General Motors Corporation, he might open a separate account for the stock under the title of General Motors Corporation Common Stock. If he also invested money in the common stock of the U. S. Steel Corporation, he might open an additional account for that stock under the title of U. S. Steel Corporation Common Stock. The usual plan, however, is to keep a summary account only entitled Corporation Stocks for all capital stock purchased for investment purposes. Such a summary account should be debited at the time of purchase for the cost price of capital stock bought, and should be credited at the time of sale for the cost price of capital stock sold. If the stock is sold at a profit, the profit may be recorded by crediting a separate account entitled Gain on Corporation Stocks. If the stock is sold at a loss, the loss may be recorded by debiting an account entitled Loss on Corporation Stocks.

If an individual purchases 100 shares of the common stock of the Master Motors Corporation through a brokerage company at a total cost of $4,950 and pays cash for it, the transaction may be recorded as indicated in the following general journal entry:

Corporation Stocks	$4,950.00	
Cash		$4,950.00
Purchased 100 shares of Master Motors common stock.		

If the stock is subsequently sold and the net proceeds of the sale amount to $5,150, the transaction may be recorded as indicated in the following general journal entry:

Cash	$5,150.00	
Corporation Stocks		$4,950.00
Gain on Corporation Stocks		200.00
Sold 100 shares of Master Motors common stock.		

If a dividend amounting to $1 per share is received while the stock is owned, the transaction may be recorded as indicated in the following general journal entry:

Cash	$100.00	
Dividends Received		$100.00
Dividends received on 100 shares of Master Motors common stock.		

The Use of the Combined Cash-Journal Illustrated. In the foregoing discussion all illustrative entries were made in general journal form. Transactions of the type discussed in this unit may, of course, be recorded in a combined cash-journal. Before a transaction is recorded in any book of original entry it should be carefully analyzed to determine its effect upon the accounting elements and to ascertain what accounts are affected. With this information no difficulty should be experienced in recording such transactions as the following in either a general journal or in a combined cash-journal:

NARRATIVE OF TRANSACTIONS

November 1. In order to obtain an extension of time on the account of Brown Bros., a 30-day, 6% note for $300 was tendered to and accepted by them.

November 10. Purchased a $100 Series E, U. S. Savings Bond, at the issue price of $75.

November 15. Received from M. D. Wright a check for $50 to apply on his account and a 30-day, 6% note for $300 in temporary settlement of the balance.

November 20. Purchased a 2½%, $1,000 U. S. Treasury Bond at the original subscription price.

December 1. Issued a check for $301.50 to Brown Bros. in payment of the principal and interest on note due today.

December 15. Received a check for $301.50 from M. D. Wright in payment of the principal and interest on his note due today.

December 15. Received $12.50 in payment of the semiannual interest on a 2½%, $1,000 U. S. Treasury Bond.

December 20. Redeemed a Series E, U. S. Savings Bond for $100. (The total appreciation in the value of the bond, amounting to $25, has already been recorded as interest income.)

December 30. Sold a 2½%, $1,000 U. S. Treasury Bond through a broker, receiving $1,133.50 in payment of the principal $1,000, and accrued interest $9, after deducting the broker's commission. The bond originally cost $1,081.60.

The foregoing transactions are shown recorded in the combined cash-journal reproduced on page 138. It should be observed that these transactions are the same as those previously discussed in this unit.

Most transactions can be recorded on one horizontal line of the combined cash-journal. However, two or more lines may be required to record some transactions. For example, to record the transaction of December 1

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COMBINED CASH-JOURNAL

CASH		DATE		DESCRIPTION	Post. Ref.	GENERAL		ACCOUNTS RECEIVABLE		ACCOUNTS PAYABLE	
RECEIPTS DR.	PAYMENTS CR.	MO.	DAY			DEBITS	CREDITS	DEBITS	CREDITS	DEBITS	CREDITS
				AMOUNTS FORWARDED							
		19— Nov.	1	Brown Bros.-Notes Payable			300 00			300 00	
	75 00		10	Government Bonds		75 00					
50 00			15	Notes Receivable-M. D. Wright		300 00			350 00		
	1000 00		20	Government Bonds		1000 00					
	301 50	Dec.	1	Notes Payable, Brown Bros.		300 00					
				Interest Expense		1 50					
301 50			15	Notes Receivable, M. D. Wright			300 00				
				Interest Income			1 50				
12 50			15	Interest Income			12 50				
100 00			20	Government Bonds			100 00				
1133 50			30	Government Bonds			1081 60				
				Interest Income			9 00				
				Gain on Government Bonds			42 90				

in the combined cash-journal, two lines were required because there were two debit entries in the General Dr. column, while in recording the transaction of December 30, three lines were required because there were three entries in the General Cr. column. Care should be exercised in writing the titles of accounts in the Description column that are affected by debit or credit entries in the General columns, because these entries must be posted individually to the proper accounts in the general ledger.

Record of Stocks and Bonds. When investments in securities such as bonds and capital stock are sufficiently numerous to justify keeping a detailed record of them, special forms similar to the one reproduced below may be used for this purpose. Such forms are produced by the leading manufacturers of loose-leaf forms and may usually be obtained through local stationery stores. The forms are so designed that all necessary information may be recorded conveniently thereon. A separate sheet should be used for keeping a record of each bond and of each stock certificate owned. A description of the bond or stock certificate, together with information regarding its purchase and sale, may be recorded on the

RECORD OF STOCKS AND BONDS

NAME U. S. Treasury Bond
DESCRIPTION #40019 K

DATE OF ISSUE June 15, 1944 DATE OF MATURITY June 15, 1969 INTEREST OR DIVIDEND 2½ PAYABLE J & D SEMI-ANNUALLY ✓
DENOMINATION $1,000.00

DATE 1944	OF WHOM PURCHASED	DATE 19__	SOLD TO	CERTIFICATE OR BOND NOS	MATURITY	PAR VALUE	PRICE PAID	TOTAL COST	SOLD FOR	INTEREST OR DIVIDENDS EARNED	LOSS OR GAIN
June	Subscription			40019 K	6/15/69	1,000	1,000	1000 00			

Illustration No. 16, Record of Stocks and Bonds

front of the form as shown in Illustration No. 16. The back of the form is ruled to facilitate recording interest or dividends received during the period of ownership.

This type of record is usually regarded as an auxiliary or memorandum record, and the information recorded on it is supplementary to the information recorded in the regular books of account.

PRACTICE ASSIGNMENT No. 12. Complete Report No. 12 in the workbook and submit your working papers to the instructor for approval. After completing the report, you may continue with the textbook discussion in Unit Six until the next report is required.

Unit Six

A SYSTEM OF ACCOUNTS FOR A RETAIL MERCHANT

XIII ACCOUNTING METHODS

A mercantile enterprise is one in which the income is derived primarily from the sale of merchandise. It is essential to good management that an adequate system of accounts be maintained. This assignment is devoted to a discussion of the accounting methods that are common to the retail merchandising type of enterprise. To make the discussion realistic, it will be related to the accounts of W. L. Mann, a retail furniture dealer.

Chart of Accounts for A Retail Merchant. W. L. Mann's chart of accounts appears on page 142. The accounts are numbered as an aid to classification and identification. The use of account numbers may save time both in journalizing transactions and in posting. In Mr. Mann's chart of accounts the numbers assigned to accounts with assets begin with 1, liabilities 2, proprietorship 3, income 4, cost 5, and expenses 6.

Account numbers beginning with 0 represent valuation accounts in which it is customary to record the estimated decrease in the value of certain assets caused by depreciation or by other factors. For example, Account No. 18 is Store Equipment, while Account No. 018 is Reserve for Depreciation of Store Equipment. To find the book value of the store equipment, the credit balance of the reserve account should be subtracted from the debit balance of the store equipment account.

It should be noted that the income accounts are classified as to (a) operating income and (b) other income. Likewise, the expense accounts are classified as to (a) operating expenses and (b) other charges. Such a classification of the accounts makes it possible to list the operating accounts separate from other accounts in the profit and loss statement. The difference between sales and sales returns and allowances is the net sales. The difference between the net sales and the cost of sales is the gross profit on sales. The difference between the gross profit on sales and the total operating expenses is the net operating income. It is desirable that this

CHART OF ACCOUNTS FOR W. L. MANN, A RETAIL MERCHANT

Note: Items in italics represent headings and not account titles.

I Assets
- *11 Cash*
  - 111 Liberty National Bank
  - 112 Petty Cash Fund
- *12 Receivables*
  - 121 Notes Receivable
  - 122 Accounts Receivable
    - 012 Reserve for Bad Debts
- *13 Investments*
  - 131 Government Bonds
- 14 Merchandise Inventory
- 15 Accrued Interest Receivable
- 16 Prepaid Insurance
- 17 Stationery and Supplies
- 18 Store Equipment
  - 018 Reserve for Depreciation of Store Equipment
- 19 Delivery Equipment
  - 019 Reserve for Depreciation of Delivery Equipment

II Liabilities
- 21 Notes Payable
- 22 Accounts Payable
- 23 Employees' Income Taxes Payable
- 24 Social Security Taxes Payable
- 25 Accrued Interest Payable

III Proprietorship
- 31 W. L. Mann, Proprietor
- 32 W. L. Mann, Drawing
- 33 Profit and Loss Summary

IV Income
- *41 Operating Income*
  - 411 Sales
    - 0411 Sales Returns and Allowances
- *42 Other Income*
  - 421 Interest Income
  - 422 Purchases Discount

V Cost
- 51 Purchases
  - 051 Purchases Returns and Allowances
- 52 Cost of Sales

VI Expenses
- *61 Operating Expenses*
  - 611 Rent Expense
  - 612 Depreciation Expense
  - 613 Loss on Bad Debts
  - 614 Advertising Expense
  - 615 Telephone and Telegraph Expense
  - 616 Heating and Lighting
  - 617 Stationery and Supplies Consumed
  - 618 Salaries and Commissions
  - 619 Social Security Taxes
  - 620 Insurance Expense
  - 621 Truck Expense
  - 622 Miscellaneous Expenses
- *63 Other Charges*
  - 631 Interest Expense
  - 632 Charitable Contributions

result be shown separately in the profit and loss statement. In arriving at the net income it is necessary to add other income to the net operating income and to subtract other charges from the sum. When the accounts are classified properly in the chart of accounts, the preparation of the financial statements is simplified.

Accounting on the Accrual Basis. The accounts of a merchant should be kept on the accrual basis. The following is quoted from the Regulations of the U. S. Treasury Department:

"In all cases in which the production, purchase, or sale of merchandise of any kind is an income-producing factor, inventories of the merchandise on hand should be taken at the beginning and end of the year and used in computing the net income of the year." (Reg. 111, Sec. 29.41-3)

"In any case in which it is necessary to use an inventory, no method of accounting in regard to purchases and sales will correctly reflect income except an accrual method." (Reg. 111, Sec. 29.41–2)

Accounting on the accrual basis for merchandise sales requires that such sales shall be treated as income of the period in which the goods are sold rather than of the period in which payment is actually received. Thus, sales should be recorded by debiting Cash or Accounts Receivable, depending on the terms, and by crediting Sales. In order that the cost of the merchandise sold will be accounted for in the same period in which the goods are sold, it is also necessary to record purchases as a debit to Purchases and as a credit to Cash or Accounts Payable, depending on the terms. Since not all of the merchandise purchased during the period may be sold during the same period, it is necessary to make adjustment for the inventories of merchandise on hand at the beginning and at the end of the period.

When the accrual method is used in accounting for purchases and sales, generally it is used also in accounting for any other income and for all expenses. Net income computed on the accrual basis may embrace amounts earned but not received and liabilities incurred but not paid. Thus, salaries accrued on December 31 but not paid until after December 31 will be treated as an expense of the year in which they accrued rather than of the year in which they were paid. Likewise, interest income accrued on December 31 but not received until after December 31 will be treated as income in the year in which it accrued rather than in the year in which it was received.

Accrued Interest Receivable. When the accounts are kept on the accrual basis, interest accrued on notes receivable and other interest-bearing obligations owned should be recorded as income for the period in which it accrues regardless of when it is collected. Since interest accrues continuously, it is impractical to keep the accounts so as to reflect the amount accrued daily. Therefore, the usual accounting practice is not to record any interest accrued until the close of the accounting period. At that time the accrued interest receivable account is adjusted for any increase or any decrease in the amount of the interest accrued on notes receivable and other interest-bearing obligations owned. Mr. Mann follows this practice, and any increase in the amount of accrued interest receivable is recorded by debiting Accrued Interest Receivable, Account No. 15, and by crediting Interest Income, Account No. 421; any decrease is recorded by debiting Interest Income, Account No. 421, and by crediting Accrued Interest Receivable, Account No. 15.

Accrued Interest Payable. When the accounts are kept on the accrual basis, interest accrued on notes payable and other interest-bearing obligations outstanding should be recorded as an expense of the period in which it accrues regardless of when it is paid. Mr. Mann follows the same plan in recording accrued interest payable as in recording accrued interest receivable. At the end of each accounting period the accrued interest payable account is adjusted for any increase or any decrease in the amount of the accrued interest on notes payable and other interest-bearing obligations outstanding. Any increase in the amount of accrued interest payable is recorded by debiting Interest Expense, Account No. 631, and by crediting Accrued Interest Payable, Account No. 25; any decrease is recorded by debiting Accrued Interest Payable, Account No. 25, and by crediting Interest Expense, Account No. 631.

Prepaid Insurance. Insurance against property loss due to fire, windstorm, burglary, and other causes may be purchased. Most policies are issued for periods of from one to five years and the premium is payable in advance. If the policy is canceled before the date of expiration, the amount of the unearned premium may be refunded to the policyholder.

When the accounts are kept on the accrual basis, insurance premiums paid should be debited to Prepaid Insurance, Account No. 16, an asset account. At the end of the period, this account should be adjusted by crediting it for the amount of the insurance expired during the period. At the same time, Insurance Expense, Account No. 620, should be debited for the amount of the insurance expired. The balance of the prepaid insurance account then represents the amount of the unexpired insurance that should be treated as a current asset.

Stationery and Supplies. In the preceding units, the cost of stationery and supplies purchased was recorded as an expense in the period in which payment was made. This is the proper procedure when the accounts are being kept on the cash basis. Since Mr. Mann keeps his accounts on the accrual basis, stationery and supplies are charged to Stationery and Supplies, Account No. 17, at the time of purchase. This is an asset account. At the end of the period, this account is adjusted by crediting it for the cost of the stationery and supplies consumed during the period. At the same time, Stationery and Supplies Consumed, Account No. 617, is debited for the amount consumed during the period.

It is important to understand that the method of recording the cost of insurance and of stationery and supplies depends upon whether the accounts are being kept on the cash basis or the accrual basis. When the accounts are kept on the cash basis, the cost of insurance and of stationery and supplies should be charged directly to appropriate expense accounts; but when the accounts are kept on the accrual basis, it is better practice to charge such costs to appropriate asset accounts. At the end of each accounting period, these two accounts should then be adjusted for the amounts expired or consumed during the period, such amounts being charged to appropriate expense accounts.

Accounts with Creditors and Customers. As previously explained, a record of the amounts due to creditors on account of credit purchases and the amounts due from customers on account of charge sales may be kept without maintaining a separate ledger account for each creditor and for each customer. Some retail merchants prefer to keep a separate ledger account for each creditor and for each customer. Even though separate ledger accounts are kept with creditors and customers, it is advisable to keep summary accounts with accounts payable and accounts receivable.

Subsidiary Ledgers. When the character of the enterprise and the volume of business are such that it is necessary to keep relatively few accounts, it may be satisfactory to keep all of the accounts together in a single general ledger, which may be bound or loose-leaf. However, when the volume of business and the number of transactions warrant employment of more than one bookkeeper to keep the records, it may be advisable to subdivide the ledger. In some businesses it is necessary to keep separate accounts with thousands of customers and creditors. In such cases it is usually considered advisable to segregate the accounts with customers and the accounts with creditors from the other accounts and to keep them in separate ledgers. When separate ledgers are kept for creditors and customers, these ledgers are known as *subsidiary ledgers.*

Balance-Column Account Form. A special account form known as the balance-column account form is widely used in keeping the individual accounts with customers and creditors. While the standard account form shown in Illustration No. 2, page 35, may be used satisfactorily for customers' and creditors' accounts, most accountants favor the use of the *balance-column account form* shown in Illustration No. 17 for such accounts. It will be noted that parallel amount columns are provided for recording debits, credits, and balances. Following each debit or credit entry the new balance may be ascertained and recorded in the Balance column, or if preferred, the balance may be ascertained and recorded at the end of each month. A Check (√) column is provided preceding the amount columns. This column may be used in checking each item recorded in the account.

In addition to providing space for entering the name and the address in the heading of the account, space is provided for entering the terms of sale and the credit rating of the customer. These two latter spaces are not used when this account form is used for creditors. When merchandise is sold on credit, the time for payment may vary, but the usual policy of most retail merchants is either to allow thirty days' credit or to require payment by a specified date, such as the tenth of the following month, for all goods sold during a month. Sometimes a discount is allowed for payment within a specified time, such as ten days. For example, the terms of sale may be "1/10, n/30," which means that the invoice is subject to a discount of 1 per cent if paid within ten days of the date of the invoice; otherwise the net amount must be paid within thirty days of the date of the invoice.

Usually some investigation is made before extending credit to a prospective customer. A merchant may establish his own credit rating system or he may use the services of some credit agency. In some cities there are local retail merchants' credit associations that supply members with credit information on prospective customers upon request. In any event, the prudent merchant will take steps to ascertain the credit record of a prospective customer before extending credit to him.

TERMS NAME
RATING ADDRESS

DATE	ITEMS	FOL.	√	DEBITS	CREDITS	BALANCE

Illustration No. 17, Balance-Column Account Form

Control Accounts. When subsidiary ledgers are kept for creditors and for customers, it is customary to keep in the general ledger summary or *control accounts* for the subsidiary ledgers. Thus, if accounts with creditors are kept in a subsidiary accounts payable ledger, a control account for accounts payable should be kept in the general ledger; if accounts with customers are kept in a subsidiary accounts receivable ledger, a control account for accounts receivable should be kept in the general ledger. The use of control accounts in the general ledger makes it possible to take a trial balance of the general ledger accounts without reference to the subsidiary ledgers.

Accounts Payable Control. The accounts payable control account provides a summary of the information recorded in the individual accounts with creditors kept in a subsidiary accounts payable ledger. Transactions affecting creditors' accounts are posted separately to the individual accounts in the subsidiary ledger. These transactions must also be posted separately, or must be summarized periodically and the totals posted, to the control account in the general ledger. The balance of the accounts payable control account may be proved by preparing a schedule of the account balances in the accounts payable ledger.

Accounts with creditors normally have credit balances. If a creditor's account has a debit balance, the balance may be circled or be written in red ink. In preparing the schedule of accounts payable, the total of accounts with debit balances should be deducted from the total of the accounts with credit balances and the difference should agree with the balance of the accounts payable control account.

Accounts Receivable Control. The accounts receivable control account provides a summary of the information recorded in the individual accounts with customers kept in a subsidiary accounts receivable ledger. Transactions affecting customers' accounts are posted separately to the individual accounts in the subsidiary ledger. These transactions must also be posted separately, or must be summarized periodically and the totals posted, to the control account in the general ledger. The balance of the accounts receivable control account may be proved by preparing a schedule of the account balances in the accounts receivable ledger.

Accounts with customers normally have debit balances. If a customer's account has a credit balance the balance may be circled or be written in red ink. In preparing the schedule of accounts receivable, the total of accounts with credit balances should be deducted from the total of the accounts with debit balances and the difference should agree with the balance of the accounts receivable control account.

Posting from the Books of Original Entry. Posting to the individual accounts with creditors and customers in the subsidiary ledgers may be done either from the books of original entry or direct from vouchers or other documents that represent the transactions. When the posting is done from the books of original entry, each item should, of course, be posted separately to the proper account and as the posting is completed the proper cross reference should be made in the Posting Reference column of the books of original entry and in the Folio column of the ledger. Under this plan the voucher or other document that represents the transaction may be filed after the transaction is recorded in the books of original entry. As each transaction is recorded in the proper book of original entry, care must be taken to enter all of the information that will be needed when posting.

Posting Direct from the Vouchers or Other Documents. When the posting is done direct from the vouchers or other documents that represent the transactions, the transactions will first be recorded in the proper books of original entry, after which the vouchers or other documents will be referred to the bookkeeper in charge of the creditors' and customers' accounts for immediate posting.

Posting to the Individual Accounts with Creditors. It is necessary to post all items that represent an increase or a decrease in the amount owed to each creditor. Following is a list of vouchers and documents that usually represent transactions completed with creditors. The usual posting reference is also indicated.

Voucher or Document	Transaction Represented	Posting Reference
(a) Purchase invoice No. 1	Purchase	P 1
(b) Credit memo	Return or allowance	CM
(c) Check stub No. 1	Payment on account	Ck 1
(d) Note issued	Temporary settlement of account	N

The purchase invoices are usually numbered consecutively as they are received. These numbers should not be confused with the numbers used by the vendor or creditor. The check stubs should be numbered consecutively to agree with the numbers of the checks issued. As the posting is completed, the proper cross reference should be made in the Folio column of the accounts and on the vouchers or documents. If a loose-leaf ledger is used and accounts with creditors are kept in alphabetic order, the posting may be indicated by means of a distinctive check mark on the voucher or document.

Posting to the Individual Accounts with Customers. It is necessary to post all items that represent an increase or a decrease in the amount owed by each customer. Following is a list of vouchers or documents that usually represent transactions completed with customers. The usual posting reference is also indicated.

Voucher or Document	Transaction Represented	Posting Reference
(a) Sale ticket No. 1	Sales	S 1
(b) Credit memo No. 1	Return or allowance	CM 1
(c) Remittances received	Payment on account	C
(d) Note received	Temporary settlement of account	N

The sales tickets usually are prepared in duplicate or triplicate and are numbered consecutively. Each sales clerk may use a different series of numbers. One copy is retained for the use of the bookkeeper and another copy is given to the customer.

Credit memorandums issued to customers in connection with sales returns or allowances are usually prepared in duplicate and are numbered consecutively. One copy goes to the customer and the other copy is retained for the use of the bookkeeper.

Remittances received from customers may consist of cash or cash items such as checks, bank drafts, and money orders. When the remittance is in the form of cash, it is customary to issue a receipt. The receipt may be issued in duplicate, in which case the duplicate copy will provide the information needed for the purpose of posting to the customer's account. Sometimes receipt stubs are used to record the information for posting purposes.

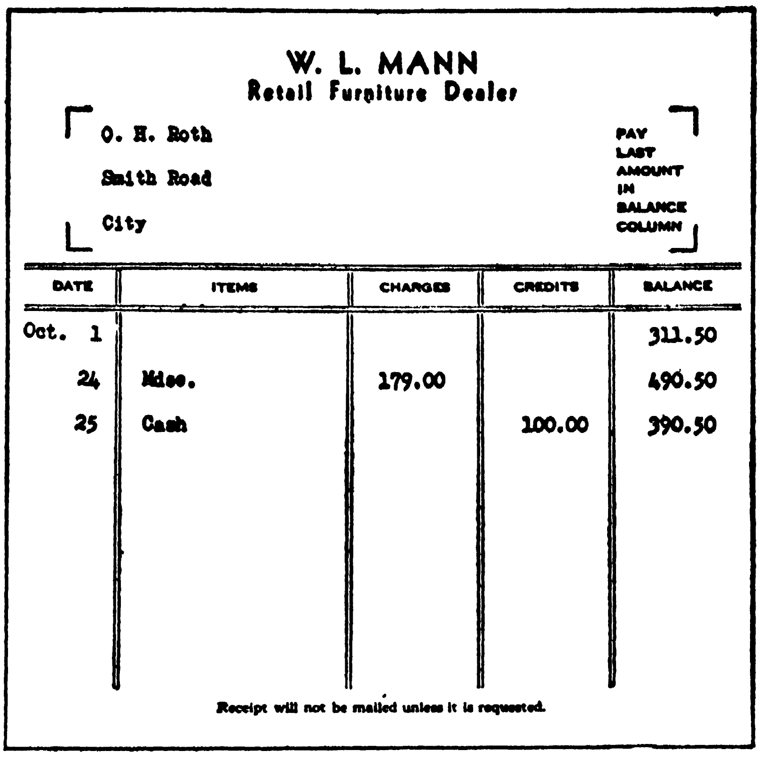
When the remittance is in the form of a check, it is not necessary to issue a receipt as the canceled check will serve as a receipt for the customer. Posting to the customer's account may be made direct from the check or from a list of checks received. Sometimes all remittances received daily are listed in such a manner as to provide the information needed for posting purposes. When this plan is followed, the bookkeeper need not handle the remittances at all. Where there are a sufficient number of employees to permit of such an organization, it is advisable to arrange the work so that the bookkeeper who posts to customers' accounts does not handle the remittances. Sometimes, however, the bookkeeper also performs the duties of a cashier, in which case the posting may be done direct to the customers' accounts from the checks, bank drafts, and money orders received.

As the posting is completed, the proper cross reference should be made in the Folio column of the account and on the vouchers or documents. If a loose-leaf ledger is used and accounts with customers are kept in alphabetic order, the posting may be indicated by means of a distinctive check mark or by initialing the voucher or document.

Accountants generally prefer this method of posting to the individual accounts with creditors and customers because it provides better control and promotes accuracy. When a purchase invoice is recorded in a purchases journal by one person and is posted directly from the invoice to the proper creditor's account by another person, it is unlikely that both persons will make the same mistake. Even if the posting is done by the person who also keeps the purchases journal, there is less likelihood of making a mistake than when the posting is done from the purchases journal. If a mistake were made in entering the amount of the invoice in the purchases journal, the same mistake would almost certainly be made in posting from the purchases journal to the creditor's account. The same reasoning may be applied to the recording of sales transactions and all other transactions that affect accounts with creditors and customers.

In most businesses, checks received from customers must be reconciled with the accounts receivable ledger before they can safely be recorded in the books of original entry. It is not uncommon for a firm to receive duplicate checks from customers or checks that are drawn incorrectly as to date, amount, or signature. In some cases, unsigned checks will be received. If a check is not found to be acceptable, for any reason, it may be considered advisable to return it to the customer with a letter of explanation.

Statement of Account. When merchandise is sold on credit, it is customary to render a statement of account to each charge customer monthly. Usually the statements are mailed as soon as they can be prepared following the close of each month. In order that statements may be mailed on the first of each month, some firms follow the policy of including transactions completed up to the 25th of the month only. Such statements are an aid to collection. When a remittance is not received from the customer within the usual credit period, a copy of the statement of account may be referred to the credit department for such action as the credit manager may wish to take. A model filled-in copy of a statement of account is reproduced in Illustration No. 18. This is a statement of the account of O. H. Roth for the month ended October 31. It shows (a) the balance at the beginning of the month amounting to $311.50; (b) a charge sale amounting to $179 made on October 24; (c) a credit amounting to $100 for cash received on October 25; and (d) the balance at the close of the month amounting to $390.50.



W. L. MANN
Retail Furniture Dealer

O. H. Roth
Smith Road
City

PAY LAST AMOUNT IN BALANCE COLUMN

DATE	ITEMS	CHARGES	CREDITS	BALANCE
Oct. 1				311.50
24	Mdse.	179.00		490.50
25	Cash		100.00	390.50

Receipt will not be mailed unless it is requested.

Illustration No. 18, Statement of Account

Accounting for Bad Debts. When merchandise is sold on credit, there is a probability that some loss may be sustained as a result of customers failing to pay their accounts in full. Experience has taught that some loss from this source is to be expected regardless of the care used in extending credit and regardless of the methods used in collecting accounts. From his past experience, a merchant usually can estimate fairly accurately the amount of loss that will be sustained on the basis of a percentage of charge sales or of outstanding accounts. It is considered good accounting practice to make provision for such loss by creating a reserve against which accounts may be charged when they prove to be uncollectible.

Reserve for Bad Debts. If it is estimated that the loss may amount to 2 per cent of the charge sales, the amount is computed at the end of the accounting period and provision therefor is made by debiting Loss on Bad Debts, Account No. 613, and by crediting Reserve for Bad Debts, Account No. 012. This results in setting up the loss in the period in which the charge sales are made, regardless of when the accounts may be ascertained to be uncollectible. When it is ascertained that an account is uncollectible, it may be charged off by debiting Reserve for Bad Debts, Account No. 012, and by crediting Accounts Receivable, Account No. 122. At the same time an entry should be made in the customer's account in the accounts receivable ledger to show that it has been charged off.

The reserve for bad debts account usually has a credit balance, and it is customary to list it in the balance sheet as a deduction from the sum of notes receivable and accounts receivable. Under this plan, if a note received from a customer proves uncollectible, it may be charged against the reserve for bad debts. In other words, a loss sustained either on accounts receivable or notes receivable is a proper charge to the reserve for bad debts. This practice is generally followed where the only notes taken are those received from customers seeking an extension of time in paying their accounts. Thus if the notes receivable account has a debit balance of $400 and the accounts receivable account has a debit balance of $12,000 and the reserve for bad debts account has a credit balance of $220, the accounts should be listed in the assets section of the balance sheet as follows:

Notes Receivable	$ 400.00	
Accounts Receivable	12,000.00	
Total	$12,400.00	
Less Reserve for Bad Debts	220.00	$12,180.00

Loss on Bad Debts. Inability to collect from a charge customer results in a loss that is usually referred to as a *loss on bad debts.* Such a loss represents a decrease in the value of the asset Accounts Receivable. As explained previously, provision for losses on bad debts may be made by debiting Loss on Bad Debts, Account No. 613, and by crediting Reserve for Bad Debts, Account No. 012. The estimated amount of such loss may be recorded monthly or at the end of each year. Under this plan, loss from bad debts is recognized and recorded as an expense of the period in which receivables arise, rather than when particular accounts are found to be worthless.

Purchases Discount. Purchase invoices representing credit purchases may be subject to discount if paid within a specified time. Retailers may be allowed a discount by wholesalers on invoices that are paid within a specified time, such as five days, ten days, or fifteen days, from the date of the invoice. This is known as a cash discount and it should not be confused with trade discounts.

Trade discounts are the discounts allowed retail dealers from the list or catalog prices of wholesalers. Such trade discounts are usually shown as a deduction on the invoice and only the net amount is recorded as the purchase price. If the invoice is subject to an additional discount for cash, it will be indicated on the invoice under the heading of "Terms." For example, the terms may be specified as "2/10, n/30," which means that if paid within ten days a discount of 2 per cent may be deducted, otherwise the net amount of the invoice is payable within thirty days.

To facilitate the payment of invoices in time to be entitled to any discount offered, Mr. Mann follows the policy of filing all invoices in an unpaid invoice file according to the due date. It is, therefore, only necessary to refer to the file each day to ascertain which invoices are due on that date and which may be subject to discount. Any amount of cash discount deducted when paying an invoice should be recorded as a credit to Purchases Discount, Account No. 422. Thus, if an invoice for $140 is subject to a discount of 2 per cent if paid within ten days and it is paid within the specified time, the payment should be recorded by debiting Accounts Payable for $140, by crediting the bank checking account for $137.20, and by crediting Purchases Discount for $2.80. The purchases discount account normally has a credit balance that is usually considered as "other income" or as "financial income." Some accountants, however, prefer to treat purchases discount as a reduction in the cost of merchandise purchased rather than as income.

Store Equipment. The cost of all equipment purchased by Mr. Mann for use in operating the store is charged to Store Equipment, Account No. 18. Thus the account is charged for the cost of all mechanical appliances, desks, chairs, tables, fixtures, showcases, etc., that are acquired for use rather than for sale. If desired, the equipment used for office purposes may be segregated from the equipment used for sales purposes by keeping separate accounts for office equipment and store equipment. Mr. Mann, however, is satisfied to keep a single summary account for all equipment used in operating his store. Supplementing this account, a card record of each item is kept.

Reserve for Depreciation of Store Equipment. Store equipment is subject to depreciation resulting from wear and tear and other factors that cause the value of the property to decrease as time elapses. Since depreciation is an expense, it is generally recorded by debiting Depreciation Expense and by crediting a reserve account for the estimated amount of depreciation sustained. Mr. Mann follows this practice and, therefore, depreciation of store equipment is recorded by debiting Depreciation Expense, Account No. 612, and by crediting Reserve for Depreciation of Store Equipment, Account No. 018.

Depreciation may be recorded monthly or at the end of the year before the financial statements are prepared. If, for example, it is estimated that store equipment depreciates at an average rate of 10 per cent a year, provision for such depreciation may be made at the end of each year by debiting Depreciation Expense and by crediting Reserve for Depreciation of Store Equipment for 10 per cent of the cost of the equipment.

Depreciation reserve accounts usually have credit balances, and it is customary to list them in the balance sheet as deductions from the asset accounts to which they apply. Thus the amount of the credit balance of Reserve for Depreciation of Store Equipment should be shown on the balance sheet as a deduction from the amount of the debit balance of Store Equipment. If, at the close of an accounting period, the store equipment account has a debit balance of $2,400 and the reserve for depreciation of store equipment account has a credit balance of $400, the accounts should be listed in the assets section of the balance sheet as follows:

Store Equipment	$2,400.00	
Less Reserve for Depreciation of Store Equipment	400.00	$2,000.00

Delivery Equipment. Some retail merchants contract for their delivery service while others maintain their own delivery trucks. Mr. Mann maintains a delivery truck, the cost of which is charged to Delivery Equipment, Account No. 19.

Reserve for Depreciation of Delivery Equipment. It is customary to keep a separate depreciation reserve account for each asset account representing property that is subject to depreciation. Since delivery equipment is depreciable property, it is, therefore, advisable to keep a separate reserve account for the depreciation of delivery equipment. Mr. Mann follows this practice; therefore depreciation of delivery equipment is recorded by debiting Depreciation Expense, Account No. 612, and by crediting Reserve for Depreciation of Delivery Equipment, Account No. 019.

If, at the close of the accounting period, the delivery equipment account has a debit balance of $1,900 and the reserve for depreciation of delivery equipment account has a credit balance of $680, the accounts should be listed in the assets section of the balance sheet as follows:

Delivery Equipment	$1,900.00	
Less Reserve for Depreciation of Delivery Equipment	680.00	$1,220.00

Depreciation Expense. The depreciation in the value of property used in operating a business enterprise represents an operating expense. The estimated amount of such depreciation may be recorded monthly or at the end of each year. As previously explained in the discussion of the reserve for depreciation accounts, Depreciation Expense is debited for the estimated amount of depreciation sustained during an accounting period, while the proper reserve accounts are credited.

Payroll Accounting. Mr. Mann has eight employees, some of whom are part-time workers. Two of his salespersons are employed on a salary and commission basis. The others are employed on a straight salary basis.

In the retail furniture business it is customary to employ salespersons on a drawing account and commission basis. Salespersons may be assigned other duties. For example, an individual might be required to devote part of his time to office work and part to sales work. Another individual might be required to devote part of his time to work as a stock clerk and the remainder to sales work. Such individuals may be paid a salary and a commission on their total net sales. The amount of the commissions earned by the salespersons is ascertained by an analysis of the sales tickets representing both cash sales and charge sales.

Mr. Mann follows the policy of paying his employees semimonthly on the fifteenth and last day of each month. His payroll procedure is as follows:

(1) The earnings of each employee for the pay period are ascertained.

(2) The amounts to be withheld from the earnings for (a) employees' income taxes and (b) federal old-age and survivors' insurance benefits are determined.

(3) The aggregate amount payable is computed by subtracting the total deductions from the total earnings of all employees, and a check for this amount is drawn on the Liberty National Bank. The payroll check is recorded in the combined cash-journal.

(4) After cashing the payroll check at the bank, the employees are then paid in cash.

Payroll Records. To meet the requirements of the various federal and state laws, it is necessary for all employers of one or more individuals to keep records to provide the following information:

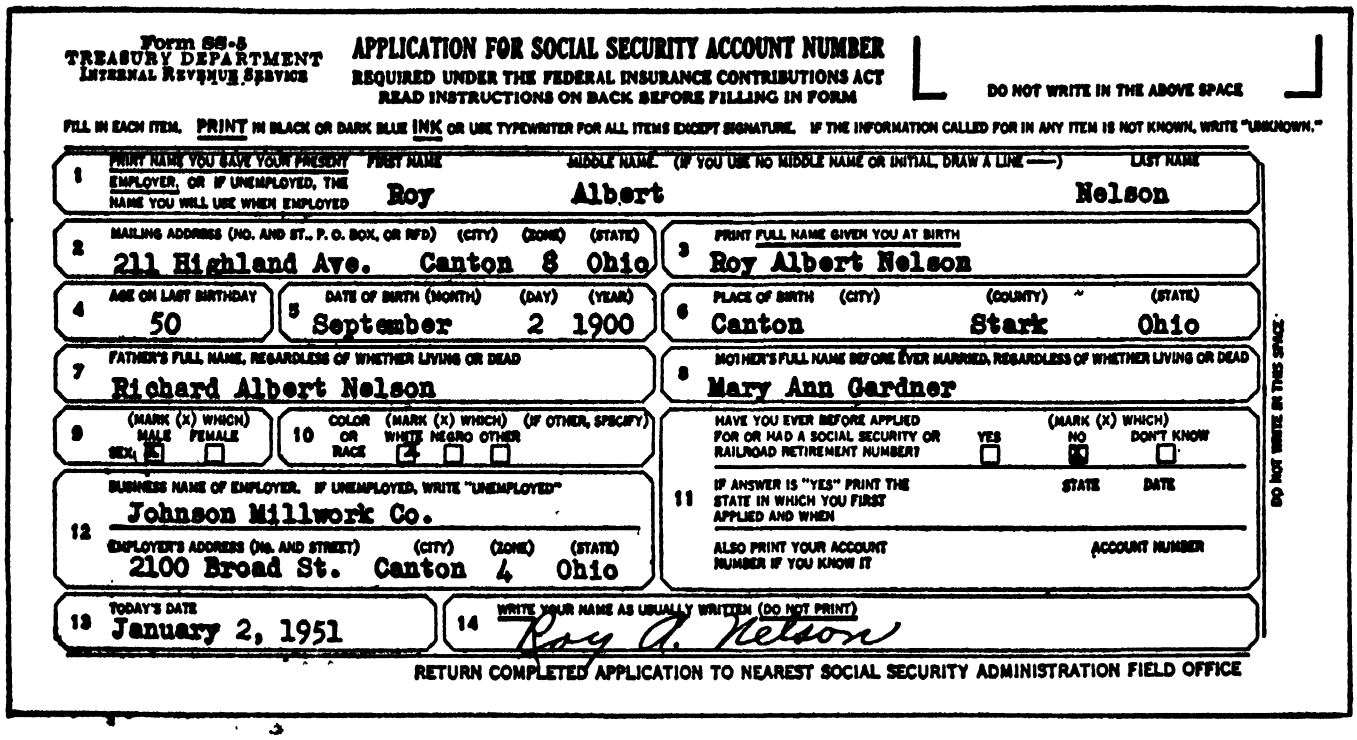
(a) Each employee's name, address, and social security account number.

(b) The gross amount of each employee's earnings, the time of payment, and the period of service covered by such payment.

(c) The amount of such earnings constituting taxable wages.

(d) The amount of the taxes withheld from each employee's earnings.

Each employee is required to have a social security account number. Form SS-5 is the required form for filing an application for an account number. A model filled-in copy of this form is reproduced below.



Form SS-5
TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE

APPLICATION FOR SOCIAL SECURITY ACCOUNT NUMBER
REQUIRED UNDER THE FEDERAL INSURANCE CONTRIBUTIONS ACT
READ INSTRUCTIONS ON BACK BEFORE FILLING IN FORM

DO NOT WRITE IN THE ABOVE SPACE

FILL IN EACH ITEM. PRINT IN BLACK OR DARK BLUE INK OR USE TYPEWRITER FOR ALL ITEMS EXCEPT SIGNATURE. IF THE INFORMATION CALLED FOR IN ANY ITEM IS NOT KNOWN, WRITE "UNKNOWN."

1 PRINT NAME YOU GAVE YOUR PRESENT EMPLOYER, OR IF UNEMPLOYED, THE NAME YOU WILL USE WHEN EMPLOYED — FIRST NAME: Roy — MIDDLE NAME (IF YOU USE NO MIDDLE NAME OR INITIAL, DRAW A LINE ——): Albert — LAST NAME: Nelson

2 MAILING ADDRESS (NO. AND ST., P. O. BOX, OR RFD) (CITY) (ZONE) (STATE): 211 Highland Ave. Canton 8 Ohio

3 PRINT FULL NAME GIVEN YOU AT BIRTH: Roy Albert Nelson

4 AGE ON LAST BIRTHDAY: 50

5 DATE OF BIRTH (MONTH) (DAY) (YEAR): September 2 1900

6 PLACE OF BIRTH (CITY) (COUNTY) (STATE): Canton Stark Ohio

7 FATHER'S FULL NAME, REGARDLESS OF WHETHER LIVING OR DEAD: Richard Albert Nelson

8 MOTHER'S FULL NAME BEFORE EVER MARRIED, REGARDLESS OF WHETHER LIVING OR DEAD: Mary Ann Gardner

9 SEX (MARK (X) WHICH): MALE [X] FEMALE [ ]

10 COLOR OR RACE (MARK (X) WHICH) (IF OTHER, SPECIFY): WHITE [X] NEGRO [ ] OTHER [ ]

11 HAVE YOU EVER BEFORE APPLIED FOR OR HAD A SOCIAL SECURITY OR RAILROAD RETIREMENT NUMBER? (MARK (X) WHICH): YES [ ] NO [X] DON'T KNOW [ ]
IF ANSWER IS "YES" PRINT THE STATE IN WHICH YOU FIRST APPLIED AND WHEN — STATE — DATE
ALSO PRINT YOUR ACCOUNT NUMBER IF YOU KNOW IT — ACCOUNT NUMBER

12 BUSINESS NAME OF EMPLOYER. IF UNEMPLOYED, WRITE "UNEMPLOYED": Johnson Millwork Co.
EMPLOYER'S ADDRESS (No. AND STREET) (CITY) (ZONE) (STATE): 2100 Broad St. Canton 4 Ohio

13 TODAY'S DATE: January 2, 1951

14 WRITE YOUR NAME AS USUALLY WRITTEN (DO NOT PRINT): Roy A. Nelson

DO NOT WRITE IN THIS SPACE

RETURN COMPLETED APPLICATION TO NEAREST SOCIAL SECURITY ADMINISTRATION FIELD OFFICE

Illustration No. 19, Application for Social Security Account Number

No specific employment records are prescribed by law for employers, but employers are required to keep records that will enable the government to ascertain whether the taxes for which the employer is liable are correctly computed and paid. Such records must be retained for a period of at least four years. Employers may design their own record forms or they may obtain suitable forms from stationery stores or firms that specialize in producing such forms. One form of payroll record is reproduced in Illustration No. 20. Mr. Mann uses such a form and each payday a record in triplicate is prepared for each employee. The original copy is retained by Mr. Mann. It provides the information needed in recording the payroll check. It also provides the information needed in preparing the required government reports. It may be filed as a permanent employee's earnings record. The second copy is given to the employee at the time wages are paid. Such a statement or receipt must be furnished to each employee from whom withholding of taxes is required. The third copy is retained by Mr. Mann as a permanent payroll record.

PAYROLL RECORD

Date ____________________ 19__

Employee's Name ____________________

Employee's S. S. No. ____________________

Payroll period Starting Ending

	SUN	MON	TUE	WED	THU	FRI	SAT	
HOURS WORKED								

	HOURS	RATE	AMOUNT
Regular time			
Overtime			
Total Earnings			

Deductions	AMOUNT	
Federal Old-Age Benefits		
State Unemployment Insurance (if any)		
Employee's Income Taxes		
Total Deductions		
Net Earnings		

I certify that this statement is correct and that I have received the wages as indicated.

Employee's Signature ____________________

Illustration No. 20, Payroll Record

The entire earnings of each employee constitute taxable wages for the purpose of determining amounts to be withheld for income tax purposes. However, only the first $3,600 of the annual earnings of each employee constitute taxable wages for the purpose of determining amounts to be withheld for old-age and survivors' insurance benefits. For example, if an employee's earnings for a given year amount to a total of $4,250, the entire amount of such earnings are subject to withholding for income tax purposes, but only the first $3,600 of such earnings are subject to withholding for old-age and survivors' insurance benefits.

Withholding Employees' Income Taxes. For federal income tax purposes, employers are required to withhold from the wages of each employee a percentage of the wages in excess of the total amount of the withholding exemptions claimed. The total amount of the exemptions claimed is arrived at by multiplying the amount of one withholding exemption by the number of exemptions claimed. The amount of one exemption is shown in the following table:

PERCENTAGE METHOD WITHHOLDING TABLE

Payroll Period	Amount of one withholding exemption
Weekly	$ 13.00
Biweekly	26.00
Semimonthly	28.00
Monthly	56.00
Quarterly	167.00
Semiannual	333.00
Annual	667.00
Daily or miscellaneous (per day of such period)	1.80

Every employee is required to furnish his employer with a signed Withholding Exemption Certificate setting forth the number of withholding exemptions that he claims. Form W-4 is the official form to be used for this certificate. A model filled-in copy of this form is reproduced in Illustration No. 21.

Reference to Illustration No. 21 will show that Mr. Mayfield claimed three exemptions. Assuming that for the semimonthly pay period ended January 15 his earnings amounted to $107.50 and that the rate of the withholding tax is 18 per cent, the amount to be withheld for income tax purposes by his employer may be computed as follows:

Total earnings for the period		$107.50
Amount of one semimonthly exemption	$28	
Number of withholding exemptions claimed	3	84.00
Excess of earnings over three withholding exemptions		$ 23.50
Rate of withholding		18%
Total amount to be withheld		$ 4.23

Form W-4

U. S. Treasury Department
Internal Revenue Service

EMPLOYEE'S WITHHOLDING EXEMPTION CERTIFICATE

(Collection of Income Tax at Source on Wages)

Print full name Richard Alan Mayfield

Print home address 912 Elm Street, Detroit, Michigan Social Security No. 259-08-9112

FILE THIS FORM WITH YOUR EMPLOYER. Otherwise, he is required by law to withhold tax from your wages without exemption.

HOW TO CLAIM YOUR WITHHOLDING EXEMPTIONS

I. If you are SINGLE, write the figure "1" .... —

II. If you are MARRIED, one exemption is allowed for the husband and one exemption for the wife.
- (a) If you claim *both* of these exemptions, write the figure "2"
- (b) If you claim *one* of these exemptions, write the figure "1"
- (c) If you claim *neither* of these exemptions, write "0" 2

III. Additional exemptions for age and blindness:
- (a) If you *or* your wife will be 65 years of age or older at the end of the year, and you claim this exemption, write the figure "1"; if *both* will be 65 or older, and you claim both of these exemptions, write the figure "2" .... —
- (b) If you *or* your wife are blind, and you claim this exemption, write the figure "1"; if *both* are blind, and you claim both of these exemptions, write the figure "2" .... —

IV. If during the year you will provide more than one-half of the support of persons closely related to you, write the number of such dependents. (See instruction 3 on other side.) 1

V. Add the number of exemptions which you have claimed above and write the total .... $\boxed{3}$

I CERTIFY that the number of withholding exemptions claimed on this certificate does not exceed the number to which I am entitled.

Dated May 1, 19 51 (Signature) Richard Alan Mayfield

Illustration No. 21, Employee's Withholding Exemption Certificate

In lieu of using the percentage method of withholding, an employer may elect to use the so-called "Wage Bracket Method" of withholding. The wage bracket method involves the use of tables in determining the amounts to be withheld. Wage bracket withholding tables covering weekly, biweekly, semimonthly, monthly, and daily or miscellaneous periods are issued by the Bureau of Internal Revenue and copies may be obtained from the office of the Collector of Internal Revenue.

Employer's Personal Income Taxes. In addition to Mr. Mann's liability for the income taxes that he is required to withhold from the wages paid to his employees, he is liable for personal income taxes. As an employer no amount is withheld at the source to pay any portion of his personal income taxes. The withholding of amounts to cover income taxes applies only to wages paid to employees in excess of their withholding exemptions. There may be little relation between Mr. Mann's personal income tax liability and his income from his business enterprise. He may have income from other sources and may have allowable deductions not related to his business. Accountants generally prefer, therefore, to treat the income taxes of a sole proprietor as a personal expense rather than as a business expense. No entry for such taxes need be made in the books of the business unless the income taxes of the proprietor are paid out of business funds, in which case the amount paid should be charged to the proprietor's drawing account.

Withholding Employees' Social Security Taxes. Under the Federal Insurance Contributions Act (FICA), taxes are imposed on both employers and employees for old-age and survivors' insurance benefits. The prescribed rates are set forth in the following table:

1939–1949, both inclusive	1%
1950–1953, both inclusive	1½%
1954–1959, both inclusive	2%
1960–1964, both inclusive	2½%
1965–1969, both inclusive	3%
After 1969	3¼%

The base of the tax is the taxable wages paid during the taxable year. The employees' portion of the tax must be withheld from their wages by the employer.

Illustration: Mr. Mayfield's earnings for the pay period ended January 15 amounted to $107.50. If the current rate of the tax is 1½ per cent, $1.61 must be withheld from his wages for old-age and survivors' insurance benefits. After withholding $4.23 for income tax purposes and $1.61 for old-age and survivors' insurance benefits, the net amount payable to Mr. Mayfield is $101.66. The net amount received by an employee is sometimes referred to as his "take-home pay."

In a few states employers are required to withhold a percentage of the employees' wages for unemployment compensation benefits, but this is not required in the state in which Mr. Mann's place of business is located.

Employer's Social Security Taxes. In addition to the employees' taxes which an employer is required to withhold from the wages of his employees for old-age and survivors' insurance benefits, a tax is imposed on the employer at the same rate. Thus, if the prevailing rate of the tax is 1½ per cent, it applies to both the employer and his employees with respect to their taxable wages. In the foregoing example, a tax of 1½ per cent, or $1.61, was withheld from the wages of Mr. Mayfield. A tax of the same amount is imposed on the employer for old-age and survivors' insurance benefits.

A tax is also imposed on employers for unemployment compensation purposes. Such taxes are imposed under both federal and state laws. Employers of eight or more individuals are subject to the federal tax.

Under the state laws the number of employees required for coverage varies from one to eight. The rate of the federal tax is 3 per cent of the taxable wages. However, where the employer is subject to state taxes imposed for unemployment compensation purposes, credit for the amount of the state taxes may be taken in computing the federal tax. Such credit is, however, limited to 90 per cent of the federal tax. Thus employers who are required to make contributions to state unemployment compensation funds may claim credit up to 2.7 per cent of the taxable wages in computing the federal tax of 3 per cent. Assuming that the total taxable wages in a given pay period amounted to $780, the taxes imposed for unemployment compensation purposes may be computed as follows:

Total taxable wages		$780.00
State U. C. Tax @ 2.7%		$ 21.06
Federal U. C. Tax @ 3%	$23.40	
Less credit for state tax	21.06	2.34
Total U. C. Tax		$ 23.40

Recording Wages and Payroll Taxes. Since Mr. Mann has eight employees, he is liable for the following payroll taxes for social security purposes:

(a) For old-age and survivors' insurance benefits —	
To be withheld from employees' wages	1½%
On employer	1½%
(b) For unemployment compensation benefits —	
State contributions	2.7%
Federal tax (3% less credit for state contributions of 2.7%)	.3%

He is also liable for the taxes that must be withheld from the wages of his employees for income tax purposes.

The following accounts are used by Mr. Mann in recording the salaries and commissions of his employees and the payroll taxes imposed on himself and his employees:

No. 618 Salaries and Commissions
No. 619 Social Security Taxes
No. 23 Employees' Income Taxes Payable
No. 24 Social Security Taxes Payable

Salaries and Commissions, Account No. 618, is an operating expense account that should be charged for the total wages and commissions earned during each pay period. At the end of the year the balance of the account represents the total salaries and commissions earned by all employees during the year.

Social Security Taxes, Account No. 619, is an operating expense account that should be charged for the taxes imposed on the employer for (a) old-age and survivors' insurance benefits and (b) unemployment compensation benefits. At the end of the year the balance of the account represents the total expense incurred because of social security taxes imposed on the employer during the year.

Employees' Income Taxes Payable, Account No. 23, is a liability account. The account should be credited each payday for the amount withheld from wages for the employees' income taxes. It should be debited for amounts paid during the year to apply on such taxes. A credit balance at the end of the year represents the amount unpaid which is a liability.

Social Security Taxes Payable, Account No. 24, is a liability account that should be credited for the social security taxes withheld from wages to cover the employees' share of the tax imposed for old-age and survivors' insurance benefits. It should be credited also for the taxes imposed on the employer for both old-age insurance benefits and unemployment compensation benefits. It should be debited for amounts paid during the year to apply on such taxes. A credit balance at the end of the year represents the amount unpaid which is a liability.

Many employers consider it advisable to keep separate liability accounts for (a) the taxes imposed for old-age and survivors' insurance benefits and (b) the taxes imposed for unemployment compensation purposes. Some also keep separate accounts for the taxes imposed by the federal and the state governments. Since the payroll records provide the detailed information needed in preparing the required reports and in paying the taxes, it is satisfactory for small businesses to keep a single account for all social security taxes payable including both those imposed on the employer and those withheld from employees' wages. This is the practice followed by Mr. Mann.

To illustrate the proper method of recording the wages and commissions earned by Mr. Mann's employees and the payroll taxes imposed on both Mr. Mann and his employees with respect to such wages and commissions, it will be assumed that the total earnings of his employees for the pay period ended September 30 amounted to $520 from which the following taxes are to be withheld:

(a) For employees' income taxes	$39.10
(b) For federal old-age and survivors' insurance benefits	7.80

From this information the payroll statement appearing at the top of the following page was prepared.

PAYROLL STATEMENT FOR PERIOD ENDED SEPTEMBER 30

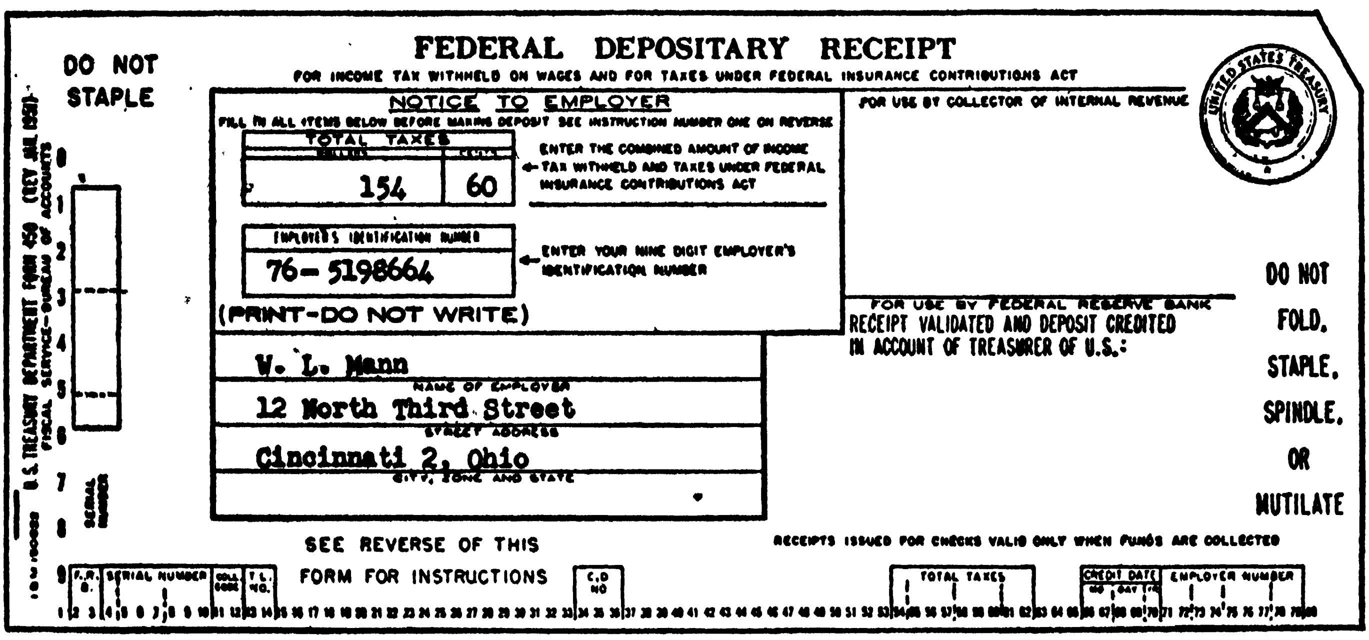
Total wages and commissions earned during period		$520.00
Employees' taxes to be withheld:		
(a) For employees' income taxes	$39.10	
(b) For old-age and survivors' insurance benefits @ 1½%	7.80	46.90
Net amount payable to employees		$473.10
Employer's payroll taxes:		
(a) For old-age and survivors' insurance benefits @ 1½%		$ 7.80
(b) For unemployment compensation benefits —		
State @ 2.7%	$14.04	
Federal (3% less state contributions of 2.7%)	1.56	15.60
Total		$ 23.40

This statement provides the information needed in recording the wages and payroll taxes. Salaries and Commissions, Account No. 618, should be debited for the total earnings of all employees for the pay period amounting to $520. Social Security Taxes, Account No. 619, should be debited for the total social security taxes imposed on the employer amounting to $23.40. Employees' Income Taxes Payable, Account No. 23, should be credited for the total amount of the income taxes withheld from employees amounting to $39.10. Social Security Taxes Payable, Account No. 24, should be credited for the total amount of the social security taxes imposed on both Mr. Mann and his employees amounting to $31.20 ($23.40 + $7.80). The Liberty National Bank, Account No. 111, should be credited for the check drawn on the bank for the net amount payable to all employees amounting to $473.10. Arranged in general journal form the entry would be as follows:

Salaries and Commissions	$520.00	
Social Security Taxes	23.40	
Employees' Income Taxes Payable		$ 39.10
Social Security Taxes Payable		31.20
Liberty National Bank		473.10

Payment of Taxes. If the amount withheld from employees' wages for income tax purposes plus the amount of the taxes imposed on both the employer and the employees for old-age and survivors' insurance benefits during any month is more than $100, it must be paid to a Federal Reserve Bank or a U. S. Depositary within fifteen days after the close of the month. However, if desired, the taxes for the last month of a calendar quarter may be remitted direct to the Collector of Internal Revenue on or before the last day of the following month. If the total amount of the taxes in any month is less than $100, monthly payment is not required. Most employers make monthly payment of the taxes either direct to a Federal Reserve Bank or a U. S. Depositary within fifteen days after the close of the month regardless of the amount. When paying the taxes it is necessary to fill in a Federal Depositary Receipt, Form 450, and to send or take it with the remittance. A model filled-in copy of this form is reproduced in Illustration No. 22. After validating the receipt, the Federal Reserve Bank will return it to the taxpayer.

The amount of the taxes imposed on employers by the state for unemployment compensation purposes must be remitted to the proper state office on or before the last day of the month following the close of each calendar quarter. The amount of the federal tax imposed on employers for unemployment compensation purposes must be paid to the Collector of Internal Revenue on or before January 31 following the close of the calendar year. The checks issued in payment of such taxes should be recorded by debiting Social Security Taxes Payable, Account No. 24, and by crediting the bank checking account.


DO NOT STAPLE

FEDERAL DEPOSITARY RECEIPT

FOR INCOME TAX WITHHELD ON WAGES AND FOR TAXES UNDER FEDERAL INSURANCE CONTRIBUTIONS ACT

NOTICE TO EMPLOYER

FILL IN ALL ITEMS BELOW BEFORE MAKING DEPOSIT SEE INSTRUCTION NUMBER ONE ON REVERSE

TOTAL TAXES: 154 | 60

ENTER THE COMBINED AMOUNT OF INCOME TAX WITHHELD AND TAXES UNDER FEDERAL INSURANCE CONTRIBUTIONS ACT

EMPLOYER'S IDENTIFICATION NUMBER: 76-5198664

ENTER YOUR NINE DIGIT EMPLOYER'S IDENTIFICATION NUMBER

(PRINT-DO NOT WRITE)

W. L. Mann
NAME OF EMPLOYER

12 North Third Street
STREET ADDRESS

Cincinnati 2, Ohio
CITY, ZONE AND STATE

FOR USE BY COLLECTOR OF INTERNAL REVENUE

FOR USE BY FEDERAL RESERVE BANK
RECEIPT VALIDATED AND DEPOSIT CREDITED IN ACCOUNT OF TREASURER OF U.S.:

DO NOT FOLD, STAPLE, SPINDLE, OR MUTILATE

SEE REVERSE OF THIS FORM FOR INSTRUCTIONS

RECEIPTS ISSUED FOR CHECKS VALID ONLY WHEN FUNDS ARE COLLECTED

TOTAL TAXES | CREDIT DATE | EMPLOYER NUMBER

Illustration No. 22, Federal Depositary Receipt

Self-Employment Tax. Beginning with the year 1951 coverage was extended to most self-employed individuals for old-age and survivors' insurance purposes. Among the self-employed individuals covered are those engaged in retail or wholesale trade, proprietors of service establishments, and persons engaged in the construction industry, manufacturing, transportation, real estate, or insurance enterprises. The rates of the self-employment tax are given at the top of the following page.

SELF-EMPLOYMENT TAX RATES

1951–1953, both inclusive.	$2\frac{1}{4}\%$
1954–1959, both inclusive.	3%
1960–1964, both inclusive.	$3\frac{3}{4}\%$
1965–1969, both inclusive.	$4\frac{1}{2}\%$
After 1969.	$4\frac{7}{8}\%$

In the case of a sole proprietor, the basis of the tax is his net business income. In the case of a partner, the basis of the tax is his distributive share of the partnership net income whether or not actually distributed. The maximum amount of income subject to tax in any year is $3,600. Self-employed persons are covered only if their net earnings from self-employment are at least $400 a year.

The self-employment tax is levied, assessed, and collected in the same manner as the federal income tax. In other words, the self-employment tax must be reported and is payable at the same time as the federal income tax. Like the personal income taxes imposed on employers, the self-employment tax is usually treated as a personal expense rather than as a business expense. The amount of the self-employment tax cannot be determined until after the net income for the year is determined and the tax is not payable until March 15 of the succeeding year. If the self-employment tax is treated as a personal expense, it need not be recorded in the books of the business unless the tax is paid out of business funds, in which case the amount paid should be charged to the proprietor's drawing account.

PRACTICE ASSIGNMENT NO. 13. Complete Report No. 13 in the workbook and submit your working papers to the instructor for approval. After completing the report, continue with the following study assignment until the next report is required.

XIV APPLICATION OF ACCOUNTING PRINCIPLES

The accrual basis of accounting as applied to a mercantile enterprise is illustrated on the following pages by reproducing the records of W. L. Mann, a retail furniture dealer. His records include the following:

(a) Books of original entry
  (1) Combined cash-journal
  (2) Purchases journal
  (3) Sales journal

(b) Books of final entry
  (1) General ledger
  (2) Accounts payable ledger
  (3) Accounts receivable ledger

(c) Auxiliary records
  (1) Petty cash disbursements record
  (2) Bank passbook
  (3) Checkbook

Combined Cash-Journal. The form of combined cash-journal used by Mr. Mann is the same as the one illustrated on page 93, except that the first two amount columns are used in recording banking transactions including deposits and checks. These columns serve the same purpose as though they were headed Cash Receipts and Payments. Mr. Mann follows the practice of depositing all cash receipts in a checking account at the Liberty National Bank and of making all disbursements by check (except for the payment of small items, which may be paid from a petty cash fund). For these reasons, a bank checking account rather than a cash account is kept in the general ledger. The posting to the bank checking account is from the combined cash-journal, the account being debited for the total receipts (deposits) and being credited for the total payments (checks).

All items entered in the General Dr. and Cr. columns of the combined cash-journal are posted individually to the proper accounts in the general ledger. No individual posting is required from any of the other amount columns. Instead, the totals of these columns are posted when the summary posting is completed at the end of the month.

Purchases Journal. The form of purchases journal used by Mr. Mann is the same as the one illustrated on page 49. It was described in detail in Unit Two. All transactions involving the purchase of merchandise on credit are recorded in this journal. Inasmuch as the posting of the credits to the accounts with creditors is done directly from the purchase invoices, the only posting required from the purchases journal is the summary posting of the total purchases for each month. This involves a debit to Purchases, Account No. 51, and a credit to Accounts Payable, Account No. 22.

Sales Journal. The form of sales journal used by Mr. Mann is the same as the one illustrated on page 54. It was described in detail in Unit Two. All transactions involving the sale of merchandise on credit are recorded in this journal. Inasmuch as the posting of charges to the accounts with customers is done directly from the sales tickets, the only posting required from the sales journal is the summary posting of the total sales for each month. This involves a debit to Accounts Receivable, Account No. 122, and a credit to Sales, Account No. 411.

General Ledger. Mr. Mann uses a general ledger with the accounts arranged in numerical order. A chart of his accounts appears on page 142. He uses the standard double-entry ledger form that is the most commonly used account form for general ledger purposes.

Accounts Payable Ledger. Mr. Mann uses an accounts payable ledger with the accounts for creditors arranged in alphabetic order. The balance-column account form is used in this ledger. Posting to the individual accounts with creditors is done direct from the vouchers or other documents. As each item is posted, the balance is extended immediately so that reference to the account of a creditor at any time will reveal the amount owed to that creditor.

Accounts Receivable Ledger. Mr. Mann uses an accounts receivable ledger with the accounts for customers arranged in alphabetic order. The balance-column account form is used in this ledger. Posting to the individual accounts with customers is done direct from the vouchers or other documents. As each item is posted, the balance is extended immediately so that reference to the account of any customer will reveal without any delay the amount due from him. This is important since it is frequently necessary to ascertain the status of a particular customer's account before extending additional credit.

Auxiliary Records. As previously stated, Mr. Mann keeps certain auxiliary records, including a petty cash disbursements record, a bank passbook, and a checkbook. The form of petty cash disbursements record is similar to that illustrated on page 119. All bank deposits are entered in the bank passbook. A record of deposits and checks issued is kept on the check stubs as well as in the combined cash-journal. At the end of each month, when the summary posting from the combined cash-journal has been completed, the balance of the bank checking account in the ledger should be the same as the bank balance recorded on the check stubs.

Accounting Procedure. The books of account containing a record of the transactions completed by Mr. Mann during the month of October are reproduced on pages 176 to 189. These books include the combined cash-journal, the purchases journal, the sales journal, the petty cash disbursements record, the general ledger, the accounts receivable ledger, and the accounts payable ledger. Before recording any transactions for October, the balance of the bank checking account was entered in the combined cash-journal, the balance in the petty cash fund was entered in the petty cash disbursements record, and the balance of each account was entered in the ledgers. These balances were obtained from the trial balance and schedules of accounts payable and accounts receivable prepared on September 30.

Reference to the accounts with customers in the accounts receivable ledger will reveal that Mr. Mann follows the practice of rating customers as to credit risk as high, good, fair, or poor. Following is a narrative of the transactions completed during October. Transactions of a type that have not been previously introduced are analyzed to show their effect upon the accounts kept by Mr. Mann.

NARRATIVE OF TRANSACTIONS

W. L. MANN, RETAIL FURNITURE DEALER

Monday, October 2

Issued checks as follows:

No. 118, Werk Realty Co., $500, in payment of October rent.

No. 119, Hayes Garage, $58.50, in payment of storage, gasoline and oil, and service.

Analysis: Both checks were recorded in the combined cash-journal. Check No. 118 was recorded by debiting Rent Expense, Account No. 611, and by crediting the bank account. Check No. 119 was recorded by debiting Truck Expense, Account No. 621, and by crediting the bank account. Note that the account titles and check numbers were written in the Description column. The account numbers were inserted in the Posting Reference column when the individual posting was completed at the end of the week.

Tuesday, October 3

Bought merchandise from the Campbell Furniture Co., Grand Rapids, $79.30, per invoice No. 21 of September 30. Terms, net 30 days.

Analysis: After receiving the merchandise and checking the invoice, it was recorded in the purchases journal. A check mark was placed in the Posting Reference column to indicate that individual posting is not done from the purchases journal. The invoice was then posted direct to the credit of the Campbell Furniture Co. in the accounts payable ledger, after which it was filed in an unpaid invoice file according to its due date.

Wednesday, October 4

Received checks from customers as follows:

Schott Decorating Co., $60.05, in full of account.

J. H. Weber, $101.75, in full of account.

Analysis: These checks were first reconciled with the accounts receivable ledger. When they were found to be for the proper amounts, they were immediately posted to the respective customers' accounts. The checks were then recorded in the combined cash-journal by debiting the bank account and by crediting Accounts Receivable, Account No. 122. The names of the customers were written in the Description column. Since the checks had already been posted to the customers' accounts, check marks were placed in the Posting Reference column.

Thursday, October 5

Sold merchandise on credit as follows:

No. 71A, J. H. Weber, 115 Main St., City, $85.

No. 57B, C. A. Anderson, 165 Willis St., City, $93.50.

No. 35C, J. N. Hook & Co., Linwood, $54.

Analysis: Unless otherwise specified, all charge sales are payable on the 10th of the following month. No cash discount is allowed. These transactions were recorded in the sales journal. A check mark was placed in the Posting Reference column to indicate that individual posting is not done from the sales journal. The sales tickets were then posted direct to the proper customers' accounts in the accounts receivable ledger, after which the tickets were filed under the name of the customer for future reference. The numbers of the sales tickets indicate that there are three sales clerks identified by the letters A, B, and C. Each of these clerks uses a separate pad of sales tickets numbered consecutively.

Friday, October 6

Issued checks as follows:

No. 120, C. J. Kramer, $53.37, in payment for circulars to be used for advertising purposes.

No. 121, National Cash Register Co., $210, in payment for a cash register.

Analysis: Both checks were recorded in the combined cash-journal by debiting the proper accounts and by crediting the bank account. Check No. 120 was charged to Advertising Expense, Account No. 614, and Check No. 121 was charged to Store Equipment, Account No. 18. The titles of the accounts to be charged and the check numbers were written in the Description column.

Bought merchandise from the Brookville Furniture Co., Brookville, $356, per invoice No. 22 of October 6. Terms, net 30 days.

Sold merchandise on credit as follows:

No. 72A, R. O. Burns, Richmond, $135.50.

No. 58B, M. D. Wright, 765 E. 9th St., City, $108.

Saturday, October 7

Total cash sales for the week, $320.

Analysis: As each cash sale was completed, a sales ticket was prepared and the amount of cash received was rung up on the cash register which automatically recorded it on a strip of tape. As each amount was thus recorded, it was added to the previous total on a mechanical accumulator in the register. Usually, the total cash sales are recorded daily, but to save time and to avoid unnecessary duplication of entries, the total cash sales are here recorded at the end of each week and on the last day of the month. This transaction was recorded in the combined cash-journal by debiting the bank account and by crediting Sales.

Made petty cash disbursements as follows:

Postage stamps, $5. Voucher No. 47.

Collect telegram, 90 cents. Voucher No. 48.

Messenger fees, $1.50. Voucher No. 49.

Analysis: All disbursements from the petty cash fund are recorded in the petty cash disbursements record. This record is ruled so as to facilitate the classification of such expenditures. It will be noted that the cost of the postage stamps was recorded as a charge to Stationery and Supplies, Account No. 17, the cost of the telegram to Telephone and Telegraph Expense, Account No. 615, and the messenger fees to Miscellaneous Expenses, Account No. 622.

END-OF-THE-WEEK WORK

(a) Proved the footings of the combined cash-journal. (b) Deposited $481.80 in the checking account at the Liberty National Bank and proved the bank balance ($7,908.97). Posted each entry individually from the General Dr. and Cr. columns of the combined cash-journal to the proper ledger accounts. (c) Proved the footings of the petty cash disbursements record and proved the balance of the petty cash fund ($92.60).

Monday, October 9

Issued checks as follows:

No. 122, Bell Telephone Co., $17.50, in payment of telephone service.

No. 123, Union Gas & Electric Co., $44.90, in payment of gas and electricity consumed during September.

No. 124, Brookville Furniture Co., $350, on account.

No. 125, Campbell Furniture Co., $300, on account.

Analysis: Checks Nos. 122 and 123 were recorded in the combined cash-journal by debiting the proper expense accounts and by crediting the bank account, the titles of the expense accounts and the check numbers being written in the Description column. Checks Nos. 124 and 125 were recorded in the combined cash-journal by debiting Accounts Payable, Account No. 22, and by crediting the bank account, the names of the creditors and check numbers being written in the Description column. Check marks were placed in the Posting Reference column to indicate that individual posting of checks issued to creditors are not posted individually from the combined cash-journal. Checks Nos. 124 and 125 were also posted direct to the creditors' accounts in the accounts payable ledger from the check stubs.

Tuesday, October 10

Issued Check No. 126 for $154.60 to the Liberty National Bank, a U. S. Depositary, in payment of the following taxes:

(a) Employees' income taxes withheld during September........		$127.20
(b) Social security taxes imposed for old-age and survivors' insurance benefits —		
On employees (withheld during September)......	$13.70	
On the employer...........................	13.70	27.40
Total..		$154.60

Analysis: The depositary receipt for this remittance is reproduced in Illustration No. 22, page 164. This transaction resulted in decreases in employees' income taxes payable and social security taxes payable with a corresponding decrease in the bank account, hence it was recorded in the combined cash-journal by debiting Employees' Income Taxes Payable, Account No. 23, for $127.20, and Social Security Taxes Payable, Account No. 24, for $27.40, and by crediting the bank account for $154.60

Sold merchandise on credit as follows:

No. 69B, Schott Decorating Co., 512 Harvard St., City, $120.

No. 41C, Peoples Hotel, Market St., City, $135.90.

No. 75A, James C. Wells, 416 Scott St., City, $62.05.

Wednesday, October 11

Received the following remittances from customers:

S. A. Burkhart, $200, on account.

E. E. Frank, $100, on account.

F. X. Vance, $15, in full of account.

West Side Furniture Exchange, $250, on account.

Thursday, October 12

Issued Credit Memorandum No. 11 for $9.10 to Peoples Hotel for merchandise returned.

Analysis: This transaction was recorded in the combined cash-journal by debiting Sales Returns and Allowances, Account No. 0411, and by crediting Accounts Receivable, Account No. 122. It was also posted direct to the account with the Peoples Hotel in the accounts receivable ledger from a carbon copy of the credit memorandum.

Made the following disbursements from the petty cash fund:

American Red Cross, $5. Voucher No. 50.

W. L. Mann, $10, for personal use. Voucher No. 51.

Friday, October 13

Received the following invoices for merchandise purchased on credit:

Kearns Furniture Co., Rosemont, $248, per invoice No. 23 of October 13. Terms, 2/10, n/30.

Robert Mitchell Furniture Co., Arlington, $199.10, per invoice No. 24 of October 12. Terms, net 30 days.

Saturday, October 14

Total cash sales for the week, $465.

Issued Check No. 127 payable to Payroll for $485.67.

Analysis: Mr. Mann follows the policy of paying his employees on the 15th and last day of each month. Since October 15 fell on Sunday, the employees were paid on the 14th. The following statement was prepared from the original copies of the payroll record of each employee's earnings (see Illustration No. 20, page 157):

Payroll Statement for Period Ended October 15

Total wages and commissions earned during period		$535.00
Employees' taxes to be withheld:		
(a) For employees' income taxes	$41.30	
(b) For old-age and survivors' insurance benefits @ 1½%	8.03	49.33
Net amount payable to employees		$485.67
Employer's payroll taxes:		
(a) For old-age and survivors' insurance benefits @ 1½%		$ 8.03
(b) For unemployment compensation benefits —		
State @ 2.7%	$14.45	
Federal (3% less state contributions of 2.7%)	1.60	16.05
Total		$ 24.08

END-OF-THE-WEEK WORK

(a) Proved the footings of the combined cash-journal. (b) Deposited $1,030 in the checking account at the Liberty National Bank and proved the bank balance ($7,586.30). (c) Posted each entry individually from the General Dr. and Cr. columns of the combined cash-journal to the proper ledger accounts. (d) Proved the footings of the petty cash disbursements record and proved the balance of the petty cash fund ($77.60).

Monday, October 16

Issued checks as follows:

No. 128, DeLuxe Upholstery Co., $400, on account.

No. 129, Barnes-Wheton Co., $201.70, in full of account.

No. 130, Kearns Furniture Co., $593.76, on account.

Tuesday, October 17

Received the following remittances from customers:

W. A. Newman, $217.60, in full of account.

W. D. Wolfe, $500, on account.

M. D. Wright, $150, on account.

Since a page of the combined cash-journal was filled after recording these remittances, the amount columns were footed and the footings proved. The totals were then recorded on the double ruled line at the bottom of the page after which they were carried forward and entered at the top of the next page.

Wednesday, October 18

Sold merchandise on credit as follows:

No. 47C, F. X. Vance, North Bend, $82.05.

No. 84A, C. E. Perry & Co., Fairmont, $484.20.

No. 70B, R. R. Philips, 524 Forest Ave., City $356.93.

Thursday, October 19

Made petty cash disbursements as follows:

Advertising, $4. Voucher No. 52.

Supplies, $6. Voucher No. 53.

Miscellaneous expenses, $1.75. Voucher No. 54.

Received the following invoices for merchandise purchased on credit:

Brown Bros., 820 Park St., City, $279.30, per invoice No. 25 of October 18. Terms, net 30 days.

King and King, 16 York St., City, $196.35, per invoice No. 26 of October 19. Terms, 2/30, n/60.

Friday, October 20

Received credit memorandum for $24.80 from Robert Mitchell Furniture Co., for merchandise returned; to be applied on invoice No. 24 received October 13.

Analysis: This transaction was recorded in the combined cash-journal by debiting Accounts Payable, Account No. 22, and by crediting Purchases Returns and Allowances, Account No. 051. It was also posted direct to the account of the Robert Mitchell Furniture Co. in the accounts payable ledger from the credit memorandum.

Saturday, October 21

Issued Check No. 131 for $250 to Mr. Mann for personal use.

Total cash sales for the week, $379.94.

END-OF-THE-WEEK WORK

(a) Proved the footings of the combined cash-journal. (b) Deposited $1,247.54 in the checking account at the Liberty National Bank and proved the bank balance ($7,388.38). (c) Posted each entry individually from the General Dr. and Cr. columns of the combined cash-journal to the proper ledger accounts. (d) Proved the footings of the petty cash disbursements record and proved the balance of the petty cash fund ($65.85).

Monday, October 23

Issued Check No. 132 for $243.04 to Kearns Furniture Co. in payment of their invoice of October 13, less 2% discount.

Analysis: The amount of the check is computed as follows:

Amount of invoice	$248.00
Discount, 2%	4.96
Balance due	$243.04

This transaction was recorded in the combined cash-journal by debiting Accounts Payable, Account No. 22, for $248 and by crediting Purchases Discount, Account No. 422, for $4.96 and crediting the bank account for

$243.04. An entry was also made in the purchases journal to record the date of payment of invoice No. 23. In posting the check direct to the account of the Kearns Furniture Co. in the accounts payable ledger the amount of the check was entered on one line and the amount of the discount on another line.

Tuesday, October 24

Sold merchandise on credit as follows:

No. 81B, J. H. Weber, 115 Main St., City, $417.75.

No. 58C, O. H. Roth, Smith Road, City, $179.

No. 59C, E. E. Frank, 875 Blair Ave., City, $298.50.

Wednesday, October 25

Received the following remittances from customers:

J. N. Hook & Co., $118.70, in payment of October 1 balance.

R. R. Philips, $200, on account.

O. H. Roth, $100, on account.

Thursday, October 26

Made petty cash disbursements as follows:

Advertising, $3. Voucher No. 55.

Supplies, $4. Voucher No. 56.

Miscellaneous expenses, $2.90. Voucher No. 57.

Friday, October 27

Issued Credit Memorandum No. 12 for $11 to R. R. Philips for merchandise returned.

Issued Check No. 133 for $170 to The Daily News in payment of advertising bill.

Issued Check No. 134 for $217.60 to the Liberty National Bank for W. A. Newman's check which was returned unpaid (N.S.F.).

Analysis: **W. A. Newman's check was received on October 17 and deposited in the bank on October 21. The bank returned the check by messenger with a notice advising that the maker did not have sufficient funds on deposit to redeem the check. Check No. 134 was recorded in the combined cash-journal by debiting Accounts Receivable, Account No. 122, and by crediting the bank account. The check was also posted immediately to Mr. Newman's account in the accounts receivable ledger.**

Saturday, October 28

Received credit memorandum for $19.30 from Brown Bros. representing an allowance on defective merchandise included in their invoice of October 18.

Total cash sales for the week, $549.37.

END-OF-THE-WEEK WORK

(a) Proved the footings of the combined cash-journal. (b) Deposited $968.07 in the checking account at the Liberty National Bank and proved the bank balance ($7,725.81). (c) Posted each entry individually from the General Dr. and Cr. columns of the combined cash-journal to the proper ledger accounts. (d) Proved the footings of the petty cash disbursements record and proved the balance of the petty cash fund ($55.95).

Monday, October 30

Received invoice from Kearns Furniture Co., Rosemont, $210, for merchandise purchased per invoice No. 27 of October 27. Terms, 2/10, n/30.

Tuesday, October 31

Received the following invoices:

Barnes-Wheton Co., Maplewood, $477.60, merchandise purchased per invoice No. 28 of October 30. Terms, 2/30, n/60.

Security Safe & Lock Co., Chicago, $400, safe purchased per invoice of October 30. Terms, 2/30, n/60.

Analysis: The invoice received from the Barnes-Wheton Co. was recorded in the purchases journal in the usual manner. The invoice received from the Security Safe & Lock Co. was recorded in the combined cash-journal by debiting Store Equipment, Account No. 18, and by crediting Accounts Payable, Account No. 22. In this enterprise the purchases journal is used only for recording invoices covering merchandise purchased on credit.

Total cash sales, $194.40.

Issued Check No. 135 payable to Payroll for $522.

PAYROLL STATEMENT FOR PERIOD ENDED OCTOBER 31

Total wages and commissions earned during period		$580.00
Employees' taxes to be withheld:		
(a) For employees' income taxes	$49.30	
(b) For old-age and survivors' insurance benefits @ 1½%	8.70	58.00
Net amount payable to employees		$522.00
Employer's payroll taxes:		
(a) For old-age and survivors' insurance benefits @ 1½%		$ 8.70
(b) For unemployment compensation benefits —		
State @ 2.7%	$15.66	
Federal (3% less state contributions of 2.7%)	1.74	17.40
Total		$ 26.10

Issued Check No. 136 for $82.94 to the State Unemployment Compensation Commission in payment of the taxes imposed during the quarter

(*Continued on page 192*)

176 COMBINED CASH-JOURNAL FOR MONTH OF October 19—

Liberty National Bank: Deposits 111 Dr.	Liberty National Bank: Checks 111 Cr.	Date: Mo.	Date: Day	Description	Post. Ref.	General: Debits	General: Credits	Accounts Receivable: 122 Dr.	Accounts Receivable: 122 Cr.	Accounts Payable: 22 Dr.	Accounts Payable: 22 Cr.
		Oct.	1	Amounts Forwarded $8249.04	✓						
	500 00		2	Rent Expense #118	611	500 00					
	58 50		2	Truck Expense #119	621	58 50					
60 05			4	Schott Decorating Co.	✓				60 05		
101 75			4	J. H. Weber	✓				101 75		
	53 37		6	Advertising Expense #120	614	53 37					
	210 00		6	Store Equipment #121	18	210 00					
320 00			7	Sales, total cash sales $7,908.97	411		320 00				
	17 50		9	Tel. & Tel. Expense #122	615	17 50					
	44 90		9	Heating & Lighting #123	616	44 90					
	350 00		9	Brookville Furniture Co. #124	✓					350 00	
	300 00		9	Campbell Furniture Co. #125	✓					300 00	
	154 60		10	Employees' Income Taxes Pay. #126	23	127 20					
				Social Security Taxes Pay.	24	27 40					
200 00			11	S. A. Burkhart	✓				200 00		
100 00			11	E. C. Frank	✓				100 00		
15 00			11	F. X. Vance	✓				15 00		
250 00			11	West Side Furniture Exchange	✓				250 00		
			12	Sales R. & A.—Peoples Hotel CM 11	0411	9 10			9 10		
465 00			14	Sales, total cash sales	411		465 00				
	485 67		14	Salaries & Commissions #127	618	535 00					
				Social Security Taxes	619	24 08					
				Employees' Income Taxes Pay.	23		41 30				
				Social Security Taxes Pay. $2,584.30	24		32 11				
	400 00		16	De Luxe Upholstery Co. #128	✓					400 00	
	201 70		16	Barnes-Wheton Co. #129	✓					201 70	
	593 76		16	Kearns Furniture Co. #130	✓					593 76	
217 60			17	W. A. Newman	✓				217 60		
500 00			17	W. D. Wolfe	✓				500 00		
150 00			17	M. D. Wright	✓				150 00		
2379 40	3370 00		17	Carried Forward	✓	1607 05	858 41		1603 50	1845 46	

W. L. Mann's Combined Cash-Journal

COMBINED CASH-JOURNAL FOR MONTH OF October 19–

177

LIBERTY NATIONAL BANK		DATE		DESCRIPTION	POST. REF.	GENERAL		ACCOUNTS RECEIVABLE		ACCOUNTS PAYABLE	
DEPOSITS 111 DR.	CHECKS 111 CR.	MO.	DAY			DEBITS	CREDITS	122 DR.	122 CR.	22 DR.	22 CR.
2379 40	3370 00	Oct.	17	AMOUNTS FORWARDED	✓	1607 05	858 41		1603 50	1845 46	
			20	Robt. Mitchell Furn. Co.–Pur. R. & A.	051		24 80			24 80	
	250 00		21	W. L. Mann, Drawing #131	32	250 00					
379 94 2759 34	3620 00		21	Sales, total cash sales $7,388.38	411	1857 05	379 94 1263 15		1603 50	1870 26	
	243 04		23	Kearns Furn. Co.–Pur. Disc. #132	422		4 96			248 00	
118 70			25	J. N. Hook & Co.	✓				118 70		
200 00			25	R. R. Philips	✓				200 00		
100 00			25	O. H. Roth	✓				100 00		
			27	Sales R. & A.–R. R. Philips C M 12	0411	11 00			11 00		
	170 00		27	Advertising Expense #133	614	170 00					
	217 60		27	W. A. Newman #134	✓			217 60			
			28	Brown Bros.–Pur. R. & A.	051		19 30			19 30	
549 37 3727 41	4250 64		28	Sales, total cash sales $7,725.81	411	2038 05	549 37 1836 78	217 60	2033 20	2137 56	
			31	Store Equipment–Security Safe & Lock Co.	18	400 00					400 00
194 40			31	Sales, total cash sales	411		194 40				
	522 00		31	Salaries & Commissions #135	618	580 00					
				Social Security Taxes	619	26 10					
				Employees' Income Taxes Pay.	23		49 30				
				Social Security Taxes Pay.	24		34 80				
	82 94		31	Social Security Taxes Pay. #136	24	82 94					
	44 05		31	W. L. Mann, Drawing #137	32	10 00					
				Stationery & Supplies	17	15 00					
				Advertising Expense	614	7 00					
				Tel. & Tel. Expense	615	90					
				Misc. Expenses	622	6 15					
3921 81	4899 63			Charitable Contributions $7,271.22	632	5 00 3171 14	2115 28	217 60	2033 20	2137 56	400 00
3921 81	4899 63					3171 14	2115 28	217 60	2033 20	2137 56	400 00
(111)	(111)					(✓)	(✓)	(122)	(122)	(22)	(22)

W. L. Mann's Combined Cash-Journal (Concluded)

178 PURCHASES JOURNAL FOR MONTH OF October 19—

Date of Entry		Date of Invoice		No. of Invoice	From Whom Purchased	Post Ref	Amount	Date Paid	
					Amount Forwarded				
Oct.	3	Sept.	30	21	Campbell Furniture Co.	✓	79.30		
	6	Oct.	6	22	Brookville Furniture Co	✓	356.00		
	13		13	23	Kearns Furniture Co	✓	248.00	Oct.	23
	13		12	24	Robt. Mitchell Furniture Co.	✓	199.10		
	19		18	25	Brown Bros.	✓	279.30		
	19		19	26	King & King	✓	196.35		
	30		27	27	Kearns Furniture Co	✓	210.00		
	31		30	28	Barnes-Wheton Co.	✓	477.60		
							2045.65		
	31				Purchases Dr. Accounts Payable Cr.	51/22	2045.65		

W. L. Mann's Purchases Journal

178 SALES JOURNAL FOR MONTH OF October 19—

Date of Entry		No. of Sale	To Whom Sold	Post Ref	Amount
			Amount Forwarded		
Oct.	5	71A	J. H. Weber	✓	85.00
	5	57B	C. A. Anderson	✓	93.50
	5	35C	J. N. Hook & Co.	✓	54.00
	6	72A	R. O. Burns	✓	135.50
	6	58B	M. D. Wright	✓	108.00
	10	69B	Schott Decorating Co.	✓	120.00
	10	41C	Peoples Hotel	✓	135.90
	10	75A	James C. Wells	✓	62.05
	18	47C	F. X. Vance	✓	82.05
	18	84A	C. E. Perry & Co.	✓	484.20
	18	70B	R. R. Philips	✓	356.93
	24	81B	J. H. Weber	✓	417.75
	24	58C	O. H. Roth	✓	179.00
	24	59C	E. E. Frank	✓	298.50
					2612.38
	31		Accounts Receivable Dr.-Sales Cr.	122/411	2612.38

W. L. Mann's Sales Journal

PETTY CASH DISBURSEMENTS FOR MONTH OF *October* **19–** 179

DAY	DESCRIPTION	VOU. NO.	TOTAL AMOUNT	DISTRIBUTION OF CHARGES #32	#17	#614	#615	#622	#632			ACCOUNT	AMOUNT
1	Brought Forward $100												
7	Postage stamps	47	5 00		5 00								
7	Collect telegram	48	90				90						
7	Messenger fees $72.60	49	1 50 7 40		5 00		90	1 50 1 50					
12	American Red Cross	50	5 00						5 00				
12	W. L. Mann Drawing $77.60	51	10 00 22 40	10 00 10 00	5 00		90	1 50	5 00				
19	Advertising	52	4 00			4 00							
19	Supplies	53	6 00		6 00								
19	Misc. expenses $65.95	54	1 75 34 15	10 00	11 00	4 00	90	1 75 3 25	5 00				
26	Advertising	55	3 00			3 00							
26	Supplies	56	4 00		4 00								
26	Misc. expenses $55.95	57	2 90 44 05	10 00	15 00	7 00	90	2 90 6 15	5 00				
			44 05	10 00	15 00	7 00	90	6 15	5 00				
31	Balance $55.95												
31	Rec'd in fund 44.05												
	Total $100.00												

W. L. Mann's Petty Cash Disbursements Record

GENERAL LEDGER

ACCOUNT *Liberty National Bank* ACCOUNT NO. *111*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		8249 04	19– Oct.	31		CJ177		4899 63
	31	7,271 22	CJ177		3921 81						
					12,170 85						

ACCOUNT *Petty Cash Fund* ACCOUNT NO. *112*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		100 00						

ACCOUNT *Notes Receivable* ACCOUNT NO. *121*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		801 50						

ACCOUNT *Accounts Receivable* ACCOUNT NO. *122*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		4118 76	19– Oct.	31		CJ177		2033 20
	31		CJ177		217 60						
	31	4,915 54	S178		2612 38						
					6948 74						

ACCOUNT *Reserve for Bad Debts* ACCOUNT NO. *012*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19– Oct.	1	Balance	✓		88 56

ACCOUNT *Merchandise Inventory* ACCOUNT NO. *14*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		28522 45						

ACCOUNT *Prepaid Insurance* ACCOUNT NO. *16*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		430 72						

ACCOUNT *Stationery and Supplies* ACCOUNT NO. *17*

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		155 00						
	31		CJ177		15 00						

W. L. Mann's General Ledger

ACCOUNT *Store Equipment* ACCOUNT No. 18

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		1850 00						
	6		CJ176		210 00						
	31		CJ177		400 00						
					2,460.00						

ACCOUNT *Reserve for Depr. of Store Equipment* ACCOUNT No. 018

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Oct.	1	Balance	✓		370 00

ACCOUNT *Delivery Equipment* ACCOUNT No. 19

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		1900 00						

ACCOUNT *Reserve for Depr. of Delivery Equipment* ACCOUNT No. 019

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Oct.	1	Balance	✓		475 00

ACCOUNT *Notes Payable* ACCOUNT No. 21

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Oct.	1	Balance	✓		2000 00

ACCOUNT *Accounts Payable* ACCOUNT No. 22

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31		CJ177		2137 56	19— Oct.	1	Balance	✓		3021 51
							31		CJ177		400 00
							31	3,329.60	P178		2045 65
											5,467.16

ACCOUNT *Employees' Income Taxes Payable* ACCOUNT No. 23

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	10		CJ176		127 20	19— Oct.	1	Balance	✓		127 20
							14		CJ176		47 30
							31	96.60	CJ177		49 30
											223.80

W. L. Mann's General Ledger (Continued)

ACCOUNT *Social Security Taxes Payable* ACCOUNT NO. 24

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	10		CJ176		27.40	19– Oct.	1	Balance	✓		140.66
	31		CJ177		82.94 110.34		14		CJ176		32.11
							31	97.23	CJ177		34.80 207.57

ACCOUNT *W. L. Mann, Proprietor* ACCOUNT NO. 31

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19– Oct.	1	Balance	✓		36,000.00

ACCOUNT *W. L. Mann, Drawing* ACCOUNT NO. 32

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		2,700.00						
	21		CJ177		250.00						
	31		CJ177		10.00 [illegible]60.00						

ACCOUNT *Sales* ACCOUNT NO. 411

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19– Oct.	1	Balance	✓		81,604.40
							7		CJ176		320.00
							14		CJ176		465.00
							21		CJ177		379.94
							28		CJ177		549.37
							31		CJ177		194.40
							31		S178		2,612.38 86,125.49

ACCOUNT *Sales Returns and Allowances* ACCOUNT NO. 0411

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		90.00						
	12		CJ176		9.10						
	27		CJ177		11.00 110.10						

ACCOUNT *Interest Income* ACCOUNT NO. 421

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19– Oct.	1	Balance	✓		42.19

W. L. Mann's General Ledger (Continued)

ACCOUNT *Purchases Discount* ACCOUNT No. 422

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Oct.	1	Balance	✓		176 50
							23		CJ177		44 96

ACCOUNT *Purchases* ACCOUNT No. 51

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		54450 17						
	31		P178		2045 65						
					56495 82						

ACCOUNT *Purchases Returns and Allowances* ACCOUNT No. 051

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
						19— Oct.	1	Balance	✓		72 00
							20		CJ177		24 80
							28		CJ177		19 30
											116 10

ACCOUNT *Rent Expense* ACCOUNT No. 611

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		4500 00						
	2		CJ176		500 00						

ACCOUNT *Advertising Expense* ACCOUNT No. 614

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		4111 75						
	6		CJ176		53 37						
	27		CJ177		170 00						
	31		CJ177		7 00						

ACCOUNT *Telephone and Telegraph Expense* ACCOUNT No. 615

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		180 00						
	9		CJ176		17 50						
	31		CJ177		90						

W. L. Mann's General Ledger (Continued)

ACCOUNT *Heating and Lighting* ACCOUNT No. 616

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		450 00						
	9		CJ176		44 90						
					494 90						

ACCOUNT *Salaries and Commissions* ACCOUNT No. 618

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		10107 80						
	14		CJ176		535 00						
	31		CJ177		580 00						
					11,222 80						

ACCOUNT *Social Security Taxes* ACCOUNT No. 619

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		454 85						
	14		CJ176		24 08						
	31		CJ177		26 10						
					505 03						

ACCOUNT *Truck Expense* ACCOUNT No. 621

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		385 00						
	2		CJ176		58 50						
					443 50						

ACCOUNT *Miscellaneous Expenses* ACCOUNT No. 622

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		369 78						
	31		CJ177		6 15						
					375 93						

ACCOUNT *Interest Expense* ACCOUNT No. 631

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		51 20						

ACCOUNT *Charitable Contributions* ACCOUNT No. 632

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		140 00						
	31		CJ177		5 00						
					145 00						

W. L. Mann's General Ledger (Concluded)

ACCOUNTS RECEIVABLE LEDGER

TERMS
RATING Good
NAME C. A. Anderson
ADDRESS 165 Willis St., City

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	5		S57B		93 50		93 50

TERMS
RATING High
NAME S. A. Burkhart
ADDRESS 2622 Euclid Ave., City

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Dr. Balance	✓				619 00
	11		C			200 00	419 00

TERMS
RATING Good
NAME R. O. Burns
ADDRESS Richmond

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	6		S72A		135 50		135 50

TERMS
RATING High
NAME E. E. Frank
ADDRESS 875 Blair Ave., City

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Dr. Balance	✓				260 00
	11		C			100 00	160 00
	24		S59C		298 50		458 50

TERMS
RATING Good
NAME J. N. Hook & Co.
ADDRESS Linwood

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Dr. Balance	✓				118 70
	5		S35C		54 00		172 70
	25		C			118 70	54 00

TERMS
RATING Poor
NAME W. A. Newman
ADDRESS 317 Sunshine Ave., City

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Dr. Balance	✓				217 60
	17		C			217 60	-0-
	27	N. S. F.	Ck135		217 60		217 60

W. L. Mann's Accounts Receivable Ledger

TERMS
RATING *Good*
NAME *Peoples Hotel*
ADDRESS *Market St., City*

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19— Oct.	10		S41C		135 90		135 90
	12		CM11			9 10	126 80

TERMS
RATING *Good*
NAME *C. E. Perry & Co.*
ADDRESS *Fairmont*

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓				101 15
	18		S84C		484 20		585 35

TERMS
RATING *High*
NAME *R. R. Philips*
ADDRESS *524 Forest Ave., City*

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓				300 00
	18		S70B		356 93		656 93
	25		C			200 00	456 93
	27		CM12			11 00	445 93

TERMS
RATING *Good*
NAME *O. H. Roth*
ADDRESS *Smith Road, City*

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓				311 50
	24		S58C		179 00		490 50
	25		C			100 00	390 50

TERMS
RATING *Good*
NAME *Schott Decorating Co.*
ADDRESS *512 Harvard St., City*

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓				60 05
	4		C			60 05	—0—
	10		J69B		120 00		120 00

W. L. Mann's Accounts Receivable Ledger (Continued)

TERMS
RATING Fair
NAME F. X. Vance
ADDRESS North Bend

DATE		ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓			15 00
	11		C		15 00	-0-
	18		S47C	82 05		82 05

TERMS
RATING Good
NAME J. H. Weber
ADDRESS 115 Main St., City

DATE		ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓			101 75
	4		C		101 75	-0-
	5		S71A	85 00		85 00
	24		S81B	417 75		502 75

TERMS
RATING Good
NAME James C. Wells
ADDRESS 416 Scott St., City

DATE		ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19— Oct.	10		S75A	62 05		62 05

TERMS
RATING Good
NAME West Side Furniture Exchange
ADDRESS Rockdale

DATE		ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓			412 41
	11		C		250 00	162 41

TERMS
RATING Fair
NAME W. D. Wolfe
ADDRESS 217 Alpine St., City

DATE		ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓			1160 00
	17		C		500 00	660 00

TERMS
RATING Fair
NAME M. D. Wright
ADDRESS 765 E. 9th St., City

DATE		ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19— Oct.	1	Dr. Balance	✓			441 60
	6		S58B	108 00		549 60
	17		C		150 00	399 60

W. L. Mann's Accounts Receivable Ledger (Concluded)

ACCOUNTS PAYABLE LEDGER

TERMS
RATING
NAME Barnes-Wheton Co
ADDRESS Maplewood

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Cr. Balance	✓				201 70
	16		Ch128		201 70		–0–
	31	10/30 – 2/30, n/60	P28			477 60	477 60

TERMS
RATING
NAME Brookville Furniture Co.
ADDRESS Brookville

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Cr. Balance	✓				350 00
	6	10/6 – n/30	P22			356 00	706 00
	9		Ch124		350 00		356 00

TERMS
RATING
NAME Brown Bros.
ADDRESS 820 Park St., City

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	19	10/18 – n/30	P25			279 30	279 30
	28		CM		19 30		260 00

TERMS
RATING
NAME Campbell Furniture Co.
ADDRESS Grand Rapids

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Cr. Balance	✓				601 05
	3	9/30 – n/30	P21			79 30	680 35
	9		Ch125		300 00		380 35

TERMS
RATING
NAME DeLuxe Upholstering Co
ADDRESS Pineville

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
19– Oct.	1	Cr. Balance	✓				800 00
	16		Ch128		400 00		400 00

W. L. Mann's Accounts Payable Ledger

TERMS
RATING

NAME Kearns Furniture Co
ADDRESS Rosemont

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
Oct	1	Cr Balance	✓				593.76
	13	10/13 – 2/10, n/30	P23			248.00	841.76
	16		CR130		593.76		248.00
	23		CR132		243.04		
	23	Discount			4.96		– 0 –
	30	10/27 – 2/10, n/30	P27			210.00	210.00

TERMS
RATING

NAME King and King
ADDRESS 16 York St., City

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
Oct	19	10/19 – 2/30, n/60	P26			196.35	196.35

TERMS
RATING

NAME Robert Mitchell Furniture Co.
ADDRESS Arlington

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
Oct	1	Cr Balance	✓				475.00
	13	10/12 – n/30	P24			199.10	674.10
	20		CM		24.80		649.30

TERMS
RATING

NAME Security Safe & Lock Co
ADDRESS Chicago

DATE		ITEMS	FOLIO	✓	DEBITS	CREDITS	BALANCE
Oct	31	10/30 – 2/30, n/60	CJ11			400.00	400.00

W. L. Mann's Accounts Payable Ledger (Concluded)

W. L. Mann's Trial Balances

Accounts	Nos.	September 30, 19— Dr. Balances	September 30, 19— Cr. Balances	October 31, 19— Dr. Balances	October 31, 19— Cr. Balances
Liberty National Bank	111	8249.04		7271.22	
Petty Cash Fund	112	100.00		100.00	
Notes Receivable	121	801.50		801.50	
Accounts Receivable	122	4118.76		4915.54	
Reserve for Bad Debts	012		88.56		88.56
Merchandise Inventory	14	28522.45		28522.45	
Prepaid Insurance	16	430.72		430.72	
Stationery & Supplies	17	155.00		170.00	
Store Equipment	18	1850.00		2460.00	
Res. for Depr. of Store Equip.	018		370.00		370.00
Delivery Equipment	19	1900.00		1900.00	
Res. for Depr. of Delivery Equip.	019		475.00		475.00
Notes Payable	21		2000.00		2000.00
Accounts Payable	22		3021.51		3329.60
Employees' Income Taxes Pay.	23		127.20		90.60
Social Security Taxes Pay.	24		140.66		97.23
W. L. Mann, Proprietor	31		36000.00		36000.00
W. L. Mann, Drawing	32	2700.00		2960.00	
Sales	411		81604.40		86125.49
Sales Returns and Allowances	0411	90.00		110.10	
Interest Income	421		42.19		42.19
Purchases Discount	422		176.50		181.46
Purchases	51	54450.17		56495.82	
Purchases Returns and Allow.	051		72.00		116.10
Rent Expense	611	4500.00		5000.00	
Advertising Expense	614	4111.75		4342.12	
Telephone & Telegraph Expense	615	180.00		198.40	
Heating & Lighting	616	450.00		494.90	
Salaries & Commissions	618	10107.80		11222.80	
Social Security Taxes	619	454.85		505.03	
Truck Expense	621	385.00		443.50	
Miscellaneous Expenses	622	369.78		375.93	
Interest Expense	631	51.20		51.20	
Charitable Contributions	632	140.00		145.00	
		124118.02	124118.02	128916.23	128916.23

W. L. Mann's Trial Balances

Schedule of Accounts Receivable

Customers	September 30, 19—	October 31, 19—
C. A. Anderson		93 50
S. A. Burkhart	619 00	419 00
R. O. Burns		135 50
E. E. Frank	260 00	458 50
J. N. Hook & Co.	118 70	54 00
W. A. Newman	217 60	217 60
Peoples Hotel		126 80
C. E. Perry & Co.	101 15	585 35
R. R. Philips	300 00	445 93
O. H. Roth	311 50	390 50
Schott Decorating Co.	60 05	120 00
F. X. Vance	15 00	82 05
J. H. Weber	101 75	502 75
James C. Wells		62 05
West Side Furniture Exchange	412 41	162 41
W. D. Wolfe	1160 00	660 00
M. D. Wright	441 60	399 60
	4118 76	4915 54

W. L. Mann's Schedule of Accounts Receivable

Schedule of Accounts Payable

Creditors	September 30, 19—	October 31, 19—
Barnes-Wheton Co.	201 70	477 60
Brookville Furniture Co.	350 00	356 00
Brown Bros.		260 00
Campbell Furniture Co.	601 05	380 35
DeLuxe Upholstery Co.	800 00	400 00
Kearns Furniture Co.	593 76	210 00
King and King		196 35
Robert Mitchell Furniture Co.	475 00	649 30
Security Safe & Lock Co.		400 00
	3021 51	3329 60

W. L. Mann's Schedule of Accounts Payable ended September 30 for unemployment compensation purposes.

Analysis: The state in which Mr. Mann's business is located levies a payroll tax of 2.7 per cent on the earnings of his employees for unemployment compensation purposes, and the taxes for each calendar quarter must be paid on or before the last day of the month following the close of the quarter. This transaction was recorded in the combined cash-journal by debiting Social Security Taxes Payable, Account No. 24, and by crediting the bank account.

Issued Check No. 137 for $44.05 to replenish the petty cash fund.

Analysis: The following statement of petty cash disbursements for October provided the information needed in recording this transaction in the combined cash-journal:

STATEMENT OF PETTY CASH DISBURSEMENTS
FOR OCTOBER

W. L. Mann, Drawing	$10.00
Stationery and Supplies	15.00
Advertising Expense	7.00
Telephone and Telegraph Expense	.90
Miscellaneous Expenses	6.15
Charitable Contributions	5.00
Total Disbursements	$44.05

Before entering the amount received to replenish the petty cash fund, the petty cash disbursements record was proved by footing the amount columns, the total was entered, and the ruling completed. The balance was then brought down below the double rules. The amount received to replenish the fund was added to the balance and the total, $100, was entered in the Description column.

END-OF-THE-MONTH WORK

(a) Proved the footings and entered the totals in the combined cash-journal. (b) Deposited $194.40 in the checking account at the Liberty National Bank and proved the bank balance ($7,271.22). (c) Completed the individual posting from the General columns of the combined cash-journal. (d) Completed the summary posting of the columnar totals of the combined cash-journal, the purchases journal, and the sales journal to the proper accounts in the general ledger. (e) Ruled the purchases and sales journals. (f) Prepared a trial balance and schedules of accounts receivable and accounts payable.

PRACTICE ASSIGNMENT No. 14. *The workbook contains an analysis test that should be completed at this time. Before beginning work on the test, this unit should be studied thoroughly. The narrative of transactions for October should be checked with the illustrations to see how each transaction is recorded and to note the effect of each transaction on the accounts involved. Special attention should be given to the analyses following certain transactions. Unless the procedure involved in recording the transactions completed by Mr. Mann during the month of October is thoroughly understood, you cannot hope to make a satisfactory grade on the test.*

Unit Seven

WORK SHEET AND FINANCIAL STATEMENTS

XV WORK SHEET

At the close of each accounting period it is desirable to analyze the accounts for the purpose of (a) determining the financial condition of the enterprise and (b) ascertaining the results of operations for the period.

The accounting period may represent a calendar year, a fiscal year, or any part of a year, such as one month, three months, or six months. Some firms divide the year into thirteen periods of four weeks each in order that the accounting periods may be of uniform length. Whatever the length of the accounting period, some analysis of the accounts is necessary as an aid to interpretation.

A trial balance is a list of all the open accounts and constitutes proof of the equality of the account balances. Although the trial balance serves a useful purpose, it does not provide information concerning either the financial condition or the results of operations in a form that is easily interpreted. Furthermore, changes that occur during the accounting period that are not represented by ordinary business transactions may not be reflected in the trial balance. For this reason some adjustments of the accounts may be necessary. As an aid in analyzing and adjusting the accounts, it is the custom of most accountants to use a work sheet.

A work sheet is sometimes referred to as a working sheet or *working trial balance.* Columnar or analysis paper should be used in preparing a work sheet. Standard analysis paper with a description column and the desired number of amount columns, ranging from two to thirty-six, is produced by the leading manufacturers of accounting forms and can usually be obtained at local stationery stores.

Function of the Work Sheet. A work sheet is an accounting device that may be used as an aid in —

(a) adjusting the accounts at the close of an accounting period,
(b) summarizing and classifying the information needed in preparing

financial statements, and

(c) ascertaining the net income or the net loss for the accounting period.

By using the work sheet as a means of ascertaining the net income or net loss for the accounting period, a check figure is obtained with which the final results shown by both financial statements — the balance sheet and the profit and loss statement — may be compared for the purpose of proof. The work sheet should not be regarded as a substitute for the trial balance, for the balance sheet, or for the profit and loss statement. The accountant ordinarily uses a work sheet for his own benefit only.

Form of the Work Sheet. A popular form of work sheet used in adjusting the accounts and in classifying the information needed in preparing a balance sheet and a profit and loss statement is a ten-column work sheet with the columns arranged as follows:

(1) Trial Balance
  (a) Debit balances
  (b) Credit balances
(2) Adjustments
  (a) Debits
  (b) Credits
(3) Adjusted Trial Balance
  (a) Debit balances
  (b) Credit balances
(4) Profit and Loss
  (a) Debit balances
  (b) Credit balances
(5) Balance Sheet
  (a) Debit balances
  (b) Credit balances

A Work Sheet for a Mercantile Enterprise. A system of accounts for a mercantile enterprise was developed in Unit Six. The accounts of W. L. Mann, a furniture dealer, are reproduced on pages 180 to 189. His accounts were kept on the accrual basis and reflect the results of operations for the ten-months' period ended October 31. Preliminary to the preparation of a balance sheet and a profit and loss statement as of that date, a ten-column work sheet was used as an aid in making the necessary adjustments of the accounts and in classifying the information needed in preparing the financial statements. This work sheet is reproduced on pages 196 and 197. Following is a discussion of the function of the amount columns appearing on the work sheet.

Trial Balance Columns. The first two amount columns in Mr. Mann's work sheet were used for the October 31 trial balance. This trial balance is reproduced on page 190.

It will be noted that certain account titles and numbers were inserted in their proper order, even though they had no balances. This was in anticipation of the adjustments to be made later. Cost of Sales was placed at the bottom of the trial balance because of the extra lines required for the adjustments.

The debit and credit amount columns were footed and the footings were entered in small pencil figures. These footings must be equal in amount to be correct.

Adjustments Columns. The third and fourth amount columns were used to make the required adjustments in the account balances. When the accounts are kept on the accrual basis, it is necessary to take into consideration the inventories at the beginning and the end of the accounting period in computing the cost of merchandise sold during the period. It is also necessary to adjust certain accounts for accruals, prepaid expenses, depreciation, and loss on bad debts.

Cost of Sales. Mr. Mann's merchandise inventory at the beginning of the accounting period, January 1, amounted to $28,522.45. The inventory at the end of the accounting period, October 31, amounted to $32,453.96. The ending inventory was recorded in the Adjustments columns of the work sheet by debiting Merchandise Inventory and by crediting Cost of Sales.

Entries were also made in the Adjustments columns to transfer (a) the beginning inventory, (b) the purchases for the period, and (c) the purchases returns and allowances for the period to the cost of sales account. This was accomplished by debiting Cost of Sales and by crediting Merchandise Inventory for $28,522.45, by debiting Cost of Sales and by crediting Purchases for $56,495.82, and by debiting Purchases Returns and Allowances and by crediting Cost of Sales for $116.10.

The results of the foregoing adjustments were that the cost of sales account was debited for (a) the amount of the inventory at the beginning of the period, $28,522.45 and (b) the amount of the purchases for the period, $56,495.82, and it was credited for (a) the amount of the inventory at the end of the period, $32,453.96 and (b) the amount of the purchases returns and allowances for the period, $116.10. The difference between the sum of the debit entries and the sum of the credit entries amounts to $52,448.21, which represents the cost of sales for the period.

Accruals. The only accruals that needed to be considered in adjusting the accounts of Mr. Mann were (a) interest accrued on notes receivable, $18.70, and (b) interest accrued on notes payable, $40.56.

The October 31 trial balance shows that Notes Receivable had a debit balance of $801.50. The note was a 6 per cent interest-bearing note,

(Continued on page 198)

W. L. Mann
Work Sheet for Ten Months' Period Ended October 31, 19–

Accounts	Acct. Nos.	Trial Balance Dr. Balances	Trial Balance Cr. Balances	Adjustments Debits	Adjustments Credits	Adj. Trial Balance Dr. Balances	Adj. Trial Balance Cr. Balances	Profit and Loss Dr. Balances	Profit and Loss Cr. Balances	Balance Sheet Dr. Balances	Balance Sheet Cr. Balances
Liberty National Bank	111	7271 22				7271 22				7271 22	
Petty Cash Fund	112	100 00				100 00				100 00	
Notes Receivable	121	801 50				801 50				801 50	
Accounts Receivable	122	4915 54				4915 54				4915 54	
Res. for Bad Debts	012		88 56		476 90		565 46				565 46
Merchandise Inventory	14	28522 45		32453 96	28522 45	32453 96				32453 96	
Accrued Interest Rec.	15			18 70		18 70				18 70	
Prepaid Insurance	16	430 72			179 47	251 25				251 25	
Stationery & Supplies	17	170 00			110 00	60 00				60 00	
Store Equipment	18	2460 00				2460 00				2460 00	
Res. for Depr. of Store Equip.	018		370 00		154 17		524 17				524 17
Delivery Equipment	19	1900 00				1900 00				1900 00	
Res. for Depr. of Del. Equip.	019		475 00		527 78		1002 78				1002 78
Notes Payable	21		2000 00				2000 00				2000 00
Accounts Payable	22		3329 60				3329 60				3329 60
Employees Income Taxes Pay.	23		90 60				90 60				90 60
Social Security Taxes Pay.	24		97 23				97 23				97 23
Accrued Interest Pay.	25				40 56		40 56				40 56
W. L. Mann, Proprietor	31		36000 00				36000 00				36000 00
W. L. Mann, Drawing	32	2960 00				2960 00				2960 00	
Sales	411		86125 49				86125 49		86125 49		
Sales Returns and Allowances	0411	110 10				110 10		110 10			
Interest Income	421		42 19		18 70		60 89		60 89		
Purchases Discount	422		181 46				181 46		181 46		
Purchases	51	56495 82			56495 82						

Purchases Returns and Allow.	051		116 10	116 10							
Rent Expense	611	5000 00				5000 00		5000 00			
Depreciation Expense	612			681 95		681 95		681 95			
Loss on Bad Debts	613			476 90		476 90		476 90			
Advertising Expense	614	4342 12				4342 12		4342 12			
Tel & Tel Expense	615	198 40				198 40		198 40			
Heating & Lighting	616	494 90				494 90		494 90			
Sta. & Sup. Consumed	617			110 00		110 00		110 00			
Salaries & Commissions	618	11222 80				11222 80		11222 80			
Social Security Taxes	619	505 03				505 03		505 03			
Insurance Expense	620			179 47		179 47		179 47			
Truck Expense	621	443 50				443 50		443 50			
Miscellaneous Expenses	622	375 93				375 93		375 93			
Interest Expense	631	51 20		40 56		91 76		91 76			
Charitable Contributions	632	145 00				145 00		145 00			
Cost of Sales	52			28522 45	32453 96						
				56495 82	116 10	52448 21		52448 21			
		128916 23	128916 23	119095 91	119095 91	130018 24	130018 24	76826 07	86367 84	53192 17	43650 40
		128916 23	128916 23	119095 91	119095 91	130018 24	130018 24	76826 07	86367 84	53192 17	43650 40
Net Income								9541 77			9541 77
								86367 84			53192 17
								86367 84	86367 84	53192 17	53192 17

Work Sheet for a Mercantile Enterprise

dated June 13, signed by Frank Zeigler. Since interest had accrued on $801.50 from June 13 to October 31, a period of 140 days at 6 per cent, it amounted to $18.70. Mr. Mann's trial balance shows that the account with Accrued Interest Receivable was in balance at the end of the period. It was, therefore, necessary to record the entire amount of the interest accrued on notes receivable by debiting Accrued Interest Receivable and by crediting Interest Income for $18.70, these entries being made in the Adjustments columns of the work sheet. This adjustment had the effect of recording the accrued interest as income of the period in which it was earned.

The October 31 trial balance shows that Notes Payable had a credit balance of $2,000. The note was a 5 per cent interest-bearing note, dated June 7, payable to the Liberty National Bank. Since interest had accrued on $2,000 from June 7 to October 31, a period of 146 days at 5 per cent, it amounted to $40.56. Mr. Mann's trial balance shows that the account with Accrued Interest Payable was in balance at the end of the period. It was, therefore, necessary to record the entire amount of the interest accrued on notes payable by debiting Interest Expense and by crediting Accrued Interest Payable for $40.56, these entries being made in the Adjustments columns of the work sheet. This adjustment had the effect of recording the accrued interest as an expense of the period in which it was incurred.

Prepaid Expenses. When the accounts are kept on the accrual basis, it may be necessary to make adjustments for certain supplies and services that were purchased in one accounting period but were partly or wholly consumed in a different accounting period. If such supplies or services are recorded as assets at the time they are purchased, the portions used or consumed during each accounting period must be recorded as expenses before the accounts are closed at the end of the period in order that the period may be charged with its proportionate part of such expenses.

Reference to Mr. Mann's chart of accounts shown on page 142 will reveal that Prepaid Insurance, Account No. 16, and Stationery and Supplies, Account No. 17, are classified as assets, while Stationery and Supplies Consumed, Account No. 617, and Insurance Expense, Account No. 620, are classified as operating expenses.

The October 31 trial balance shows that Prepaid Insurance had a debit balance of $430.72. This was the amount of the premium paid on a two-year policy issued January 2 of the current year. On October 31 ten months had elapsed; thus, the current period ending October 31 should be charged with five-twelfths of the premium paid or $179.47. This represents the value of the insurance expired during the period. The expired insurance was recorded in the Adjustments columns of the work sheet by debiting Insurance Expense, Account No. 620, and by crediting Prepaid Insurance, Account No. 16, for $179.47. This adjustment had the effect of recording the insurance expired during the period as an expense of the period in which it was incurred.

The October 31 trial balance shows that Stationery and Supplies had a debit balance of $170. An inventory taken on October 31 shows that stationery and supplies on hand, unused, amounted to only $60. This indicates that the stationery and supplies consumed during the period must have amounted to $110 ($170 — $60). This was recorded in the Adjustments columns of the work sheet by debiting Stationery and Supplies Consumed, Account No. 617, and by crediting Stationery and Supplies, Account No. 17, for $110. This adjustment had the effect of recording the stationery and supplies consumed during the period as an expense of the period in which it was incurred.

Depreciation. A decrease in the value of property caused by wear and tear resulting from its use or from mere lapse of time is commonly referred to as *depreciation.* Any depreciation sustained should be recorded as an expense of the period in which it occurs. The amount of the depreciation sustained is usually estimated on a basis of past experience. The assets of Mr. Mann that are subject to depreciation include store equipment and delivery equipment. He estimates that these assets depreciate at the following rates based on cost:

(a) Store equipment, 10% a year.
(b) Delivery equipment, 33⅓% a year.

The amount of depreciation recorded on the work sheet was computed as follows:

Store Equipment $1,850* at 10% for 10 months	$154.17
Delivery Equipment $1,900 at 33⅓% for 10 months	527.78
Total depreciation for 10 months	$681.95

The depreciation was recorded on the work sheet by debiting Depreciation Expense, Account No. 612, for $681.95 and by crediting Reserve for Depreciation of Store Equipment, Account No. 018, for $154.17 and Reserve for Depreciation of Delivery Equipment, Account No. 019, for $527.78.

*Mr. Mann does not consider it advisable to compute depreciation on any property owned less than a month. Hence, no depreciation was recorded on the store equipment purchased October 6 at a cost of $210 and October 31 at a cost of $400.

Loss on Bad Debts. In adjusting the accounts at the close of an accounting period, it is customary to make provision for any anticipated losses on notes receivable and accounts receivable. Mr. Mann follows the practice of adding to the reserve for bad debts an amount equal to 1 per cent of the charge sales. His charge sales for the ten-months' period amounted to $47,690. One per cent of $47,690 equals $476.90. This was recorded in the Adjustments columns of the work sheet by debiting Loss on Bad Debts, Account No. 613, and by crediting Reserve for Bad Debts, Account No. 012, for $476.90. This adjustment had the effect of recording the anticipated loss on bad debts as an expense of the period in which the merchandise was sold. This is considered a more conservative accounting practice than to wait until an account proves uncollectible to record the loss.

After making the required entries in the Adjustments columns of the work sheet, the columns were footed and the footings were entered in small pencil figures. These footings must be equal in amount.

Adjusted Trial Balance Columns. The fifth and sixth amount columns of the work sheet were used for the adjusted trial balance. To ascertain the balance of each account after making the required adjustments, it is necessary to take into consideration the amounts recorded in the first four amount columns. When an account is not affected by entries in the Adjustments columns, the balance recorded in the Trial Balance columns should be extended to the Adjusted Trial Balance columns. The amounts of the debit balances should be listed in the fifth column, and the amounts of the credit balances should be listed in the sixth column.

When an account is affected by an entry in the Adjustments columns, the balance recorded in the Trial Balance columns is increased or decreased, as the case may be, by the amount of the adjusting entry; the adjusted balance should be extended to the proper Adjusted Trial Balance column. For example, Reserve for Depreciation of Store Equipment is listed in the Trial Balance columns with a credit balance of $370. Since there is a credit entry of $154.17 in the Adjustments columns, the amount to be extended to the Adjusted Trial Balance Cr. column is ascertained by addition ($370 + $154.17 = $524.17). Prepaid Insurance is listed in the Trial Balance columns with a debit balance of $430.72. Since there is a credit entry of $179.47 in the Adjustments columns, the amount to be extended to the Adjusted Trial Balance Dr. column is ascertained by subtraction ($430.72 − $179.47 = $251.25.)

The Adjusted Trial Balance columns were footed and the footings were entered in small pencil figures. These footings must be equal in amount to be correct.

Profit and Loss Columns. The seventh and eighth amount columns of the work sheet were used to classify the temporary proprietorship accounts. These accounts are sometimes referred to as *nominal accounts.* Debit balances should be listed in the seventh amount column. Accounts with debit balances include Sales Returns and Allowances, all expense accounts, other charges, and Cost of Sales. Credit balances should be listed in the eighth amount column. Accounts with credit balances include Sales and all other income accounts.

The Profit and Loss amount columns were footed and the footings were entered in small pencil figures. The difference between the footings of these columns constitutes the amount of the net increase or the net decrease in proprietorship for the accounting period. If the total of the credit balances exceeds the total of the debit balances, the difference represents a net increase in proprietorship. On the other hand, if the total of the debit balances exceeds the total of the credit balances, the difference represents a net decrease in proprietorship. A net increase in proprietorship is usually referred to as the net income for the accounting period, while a net decrease in proprietorship is usually referred to as the net loss for the accounting period.

Reference to the Profit and Loss columns of Mr. Mann's work sheet will show that the total of the credit balances amounted to $86,367.84 and the total of the debit balances amounted to $76,826.07. The difference, amounting to $9,541.77, represented the amount of his net income for the ten-months' period.

Balance Sheet Columns. The ninth and tenth amount columns of the work sheet were used to classify the assets, the liabilities, and the permanent proprietorship accounts. Asset and liability accounts are sometimes referred to as *real accounts.* The debit balances should be recorded in the ninth amount column. The credit balances should be recorded in the tenth amount column.

The Balance Sheet columns were footed and the footings were entered in small pencil figures. The difference between the footings of these columns constitutes the amount of the net increase or the net decrease in proprietorship for the accounting period. If the total of the debit balances exceeds the total of the credit balances, the difference represents a net income for the accounting period. On the other hand, if the total of the credit balances exceeds the total of the debit balances, the difference represents a net loss for the period. This difference should be the same as the difference between the footings of the Profit and Loss columns.

Reference to the Balance Sheet columns of the work sheet will show that the total of the debit balances amounted to $53,192.17 and the total of the credit balances amounted to $43,650.40. The difference of $9,541.77 represented the amount of his net income for the ten-months' period.

Totaling and Ruling the Work Sheet. After extending the adjusted account balances into the proper amount columns, all of the columns should be totaled and ruled. The difference between the totals of the Profit and Loss columns and the totals of the Balance Sheet columns should be recorded on the next ruled line immediately below the totals. If the difference represents a net increase in proprietorship, it should be labeled "Net Income" and the amount should be recorded in the seventh and tenth amount columns. If the difference represents a net decrease in proprietorship, it should be labeled "Net Loss" and the amount should be recorded in the eighth and ninth amount columns.

Proving the Work Sheet. There are two ways of proving the accuracy of the work sheet, as follows:

(a) The net income or the net loss, represented by the difference between the footings of the Profit and Loss columns, should agree with the difference between the footings of the Balance Sheet columns.

(b) After the net income or the net loss has been recorded in the proper amount columns, the footings of the Profit and Loss columns should be equal in amount; the footings of the Balance Sheet columns should also be equal in amount.

The final test of the accuracy of the work sheet is the equality of the footings of each pair of amount columns. When the work sheet has been completed and proved, the net income or the net loss shown thereon will serve as a check figure with which the results of both financial statements — the balance sheet and the profit and loss statement — may be compared for the purpose of proof. The most common type of error in preparing a work sheet is to classify the account balances incorrectly as they are extended to the Profit and Loss or Balance Sheet columns. When an account balance is improperly classified, the error will be reflected in the amount of the net income or the net loss. The difference between the Profit and Loss columns must be the same as the difference between the Balance Sheet columns before the amount is entered as the net income or the net loss.

At the close of the accounting period, the proprietor's capital or net worth may be ascertained by analyzing the asset and the liability accounts. The amount of the net increase or the net decrease in proprietorship may be ascertained by a comparison of the amount of the proprietorship at the close of the accounting period with the amount of the proprietorship at the beginning of the accounting period. If there have been no withdrawals by the proprietor during the period, the amount of the net increase in proprietorship will equal the net income for the period or the amount of the net decrease in proprietorship will equal the net loss for the period. If the proprietor has made withdrawals during the accounting period, the amount of such withdrawals should be added to the net increase in proprietorship to find the net income for the period or the amount of the withdrawals should be subtracted from the net decrease in proprietorship to ascertain the net loss for the period.

The net income or the net loss for the period may also be ascertained by analyzing the income and the expense accounts. The amount of the net income or the net loss should be the same regardless of which of these methods is used.

Reference to the work sheet reproduced on pages 196 and 197 will reveal that the accounts have been classified in a manner that shows the net results of the operations for the accounting period. The preparation of such a work sheet is a preliminary step in preparing a balance sheet and a profit and loss statement.

> ***PRACTICE ASSIGNMENT No. 15. Complete Report No. 15 in the workbook and submit your working papers to the instructor for approval. After completing the report, continue with the following study assignment until the next report is required.***

XVI THE BALANCE SHEET

Assets, liabilities, and proprietorship constitute the accounting elements. A detailed statement of these elements, showing the amount of each asset, the amount of each liability, and the amount of the proprietor's present capital or present worth is known as a *balance sheet*. The title of such a statement had its origin in the equality of the elements, that is, in the balance between the sum of the assets and the sum of the liabilities and the proprietorship.

Function of the Balance Sheet. The balance sheet is a formal report of assets, liabilities, and proprietorship as of a specified date. It is sometimes known as a statement of assets and liabilities or as a statement of resources and liabilities.

A balance sheet may be prepared to show the financial status of any entity, whether its character be that of an individual proprietorship, a partnership, a corporation, or any other unit such as a syndicate, an association, or an estate. A balance sheet for an individual may represent his financial status as an individual or it may set forth the financial status of a particular enterprise that he is conducting. An individual may conduct more than one business or enterprise, and balance sheets may be prepared to show the financial status of each business or enterprise separately.

The primary function of a balance sheet is to provide financial information for those who desire it. For example:

(a) An individual may desire to know (1) the book value of his property; (2) the amount of his debts; and (3) his present worth, that is, his equity in what he owns or the amount of his investment in a business enterprise.

(b) A creditor or a credit agency may request a balance sheet as an aid in determining credit limitations. Before credit is extended, it is customary to make inquiry regarding the financial status of an individual based on his ability to make payment at the time and under the conditions stipulated.

(c) A bank or other financial institution may require a balance sheet from one who is seeking a loan. Such institutions extend credit based upon the financial condition and the reputation of the borrower for prompt payment of debts.

(d) A prospective purchaser of a business or of a part interest in a business may desire a balance sheet of the enterprise as an aid in determining the present worth of the business.

Form of the Balance Sheet. A balance sheet may be prepared either (a) in account form or (b) in report form. Whichever of these forms is used, the heading should be the same and should consist of the following:

(a) Name of the individual, firm, or company.
(b) Title of the report.
(c) Date of the report.

The name of the individual, firm, or company should be stated in full in the heading. It is necessary to date a balance sheet because it reports the financial status of the individual, firm, or company as of the close of business on the date specified. The date specified in the heading of a balance sheet should be the last day of an accounting period regardless of whether the period ends on a regular business day, a Sunday, or a holiday. For instance, if the accounting period is for a calendar year, the date of the balance sheet should be December 31 even though that date may fall on Sunday.

A balance sheet is said to be arranged in account form when the assets are listed on the left side and the liabilities and the proprietorship are listed on the right side. Some persons consider the account form of balance sheet to be more technical than the report form. This is not necessarily true. Generally accountants and businessmen who have a knowledge of accounting prefer the account form of balance sheet. The balance sheet reproduced on page 206 is arranged in account form.

A balance sheet is said to be arranged in report form when the items are listed vertically — the assets first, the liabilities second, and the proprietorship third. The balance sheet reproduced on page 207 is arranged in report form.

In each illustration the sum of the assets equals the sum of the liabilities plus the proprietorship.

A balance sheet may be penwritten on ruled paper as illustrated on page 206 or it may be typed on plain bond paper as shown on page 207. The information needed in preparing the balance sheet for Mr. Mann was obtained from his work sheet.

Classification of the Accounts in the Balance Sheet. One of the functions of the work sheet is to classify the information needed in preparing financial statements. Reference to the work sheet reproduced on pages 196 and 197 will show that the accounts are classified into two groups as follows:

(a) Profit and loss accounts.
(b) Balance sheet accounts.

A further classification of asset, liability, and proprietorship accounts may be made in preparing the balance sheet.

Asset Accounts. Accounts representing the asset element may be divided into two classes as follows:

(a) Current assets.
(b) Fixed assets.

Current Assets. For accounting purposes, current assets include cash and all other assets that may be reasonably expected to be realized in cash or sold or consumed during the normal operating cycle of the business. The ordinary operations of a mercantile enterprise involve the

(Continued on page 207)

W. L. Mann

Balance Sheet, October 31, 19–

Assets				Liabilities			
Current Assets:				Current Liabilities.			
Cash		7371 22		Notes Payable		2000 00	
Notes Receivable	801 50			Accounts Payable		3329 60	
Accounts Receivable	4915 54			Employees Income Taxes Pay.		90 60	
Total	5717 04			Social Security Taxes Pay.		97 23	
Less Res. for Bad Debts	565 46	5151 58		Accrued Interest Payable		40 56	
Merchandise Inventory		32453 96		Total Current Liabilities			5557 99
Accrued Interest Receivable		18 70		Proprietorship			
Prepaid Insurance		251 25		W. L. Mann, Proprietorship			
Stationery & Supplies		60 00		January 1, 19–		36000 00	
Total Current Assets			45306 71	Net Income	9541 77		
Fixed Assets:				Less Withdrawals	2960 00	6581 77	
Store Equipment	2460 00			Proprietorship, Oct 31, 19–			42581 77
Less Res. for Depr.	524 17	1935 83					
Delivery Equipment	1900 00						
Less Res. for Depr.	1002 78	897 22					
Total Fixed Assets			2833 05				
Total Assets			48139 76	Total Liabilities & Prop.			48139 76

Balance Sheet—Account Form

W. L. MANN

BALANCE SHEET, OCTOBER 31, 19--

ASSETS

Current Assets:			
Cash		$ 7,371.22	
Notes Receivable	$ 801.50		
Accounts Receivable	4,915.54		
Total	$5,717.04		
Less Reserve for Bad Debts	565.46	5,151.58	
Merchandise Inventory		32,453.96	
Accrued Interest Receivable		18.70	
Prepaid Insurance		251.25	
Stationery and Supplies		60.00	
Total Current Assets			$45,306.71
Fixed Assets:			
Store Equipment	$2,460.00		
Less Reserve for Depreciation	524.17	$ 1,935.83	
Delivery Equipment	$1,900.00		
Less Reserve for Depreciation	1,002.78	897.22	
Total Fixed Assets			2,833.05
Total Assets			$48,139.76

LIABILITIES

Current Liabilities:			
Notes Payable		$ 2,000.00	
Accounts Payable		3,329.60	
Employees' Income Taxes Payable		90.60	
Social Security Taxes Payable		97.23	
Accrued Interest Payable		40.56	
Total Current Liabilities			$ 5,557.99

PROPRIETORSHIP

W. L. Mann, Proprietorship, January 1, 19--		$36,000.00	
Net Income	$9,541.77		
Less Withdrawals	2,960.00	6,581.77	
Proprietorship, October 31, 19--			42,581.77
Total Liabilities and Proprietorship			$48,139.76

Balance Sheet — Report Form

expenditure of cash for merchandise, supplies, and services. The merchandise may be sold for cash or on credit resulting in accounts receivable and, in some instances, notes receivable. The receivable accounts ultimately are converted into cash. The average time intervening between the acquisition of merchandise and the final cash realization constitutes an operating cycle. Where the period of the operating cycle is less than twelve months, a one-year time period should be used in segregating current assets; but where the cycle is in excess of twelve months, as in the tobacco and lumber businesses, the longer period should be used. In a mercantile enterprise the current assets usually will include cash, marketable securities, receivables, merchandise inventory, and prepaid expenses such as prepaid insurance unexpired and unused supplies.

The asset cash may be represented by one or more accounts, such as bank checking accounts, bank savings accounts, and a petty cash fund. Reference to Mr. Mann's balance sheet will show that cash is listed at $7,371.22. Reference to his work sheet will show that this is made up of two items including the balance in the checking account at the Liberty National Bank, $7,271.22 and the amount of the petty cash fund, $100.

Marketable securities may be represented by one or more accounts such as government bonds, corporation bonds, and corporation stocks. For securities to be readily marketable, there must be an existing market where they can be sold at prevailing prices without undue delay. All securities that are listed on stock exchanges, such as the New York Stock Exchange, the Midwest Stock Exchange, the San Francisco Stock Exchange, or any other local stock exchange, may usually be bought or sold at prevailing market prices without delay.

To list its securities on any stock exchange, the issuing company must meet the regulations of the exchange as well as the regulations prescribed by federal and state laws. When a company's securities are approved by such an exchange for listing, brokers who are members of that exchange may then execute transactions in behalf of their customers for the purchase or the sale of such securities.

Securities may be marketable even though they are not listed on any security exchange. It is not difficult to ascertain whether securities are marketable. Inquiries at brokers' offices, banks, or investment houses will usually reveal whether or not there is a market for any particular security.

Receivables may include notes receivable, accounts receivable, and other receivables representing current assets.

Services and supplies purchased in one period may be only partially consumed during that period. Such items are commonly referred to as prepaid expenses. If not actually paid for in advance, the amount owed would be included in accounts payable; hence payment would require the use of current assets during the operating cycle. Accountants generally prefer to classify the unexpired portion of prepaid insurance, unused supplies and other prepaid expenses as current assets.

Reference to the balance sheet of Mr. Mann, reproduced on pages 206 and 207, will reveal that cash, notes receivable, accounts receivable, merchandise inventory, accrued interest receivable, prepaid insurance, and stationery and supplies are classified as current assets.

Fixed Assets. Property that is used in the operation of a mercantile enterprise, such as office equipment, store equipment, and delivery equipment, constitutes fixed assets. Buildings and land that are owned and used for business purposes also constitute fixed assets.

Reference to Mr. Mann's balance sheet will show that store equipment and delivery equipment are classified as fixed assets. The fixed assets are listed in the balance sheet at cost and the reserves for depreciation are listed as deductions from the cost. The difference between the cost of any asset and the amount of its reserve for depreciation represents the *book value* of the asset.

Liability Accounts. Accounts representing the liability element may be divided into two classes as follows:

(a) Current liabilities.
(b) Fixed liabilities.

Current Liabilities. Current liabilities include those obligations that mature in a comparatively short period of time or that will become payable within the normal operating cycle of the business. Reference to Mr. Mann's balance sheet will show that notes payable, accounts payable, employees' income taxes payable, social security taxes payable, and accrued interest payable are classified as current liabilities.

Fixed Liabilities. Fixed liabilities include those obligations that do not mature within the normal operating cycle of the business. The most common of the fixed liabilities is mortgages payable.

A mortgage payable is a debt or an obligation that is secured by a *mortgage,* which provides for the conveyance of certain property upon failure to pay the debt at maturity. When the debt is paid, the mortgage becomes void. It will be seen, therefore, that a mortgage payable differs little from an account payable or a note payable except that the creditor holds the mortgage as security for the payment of the debt. Usually debts secured by mortgages run for a longer period of time than ordinary notes payable or accounts payable. A mortgage payable should be classed as a fixed liability only in case the maturity date extends beyond a year or beyond the normal operating cycle of the business. In other words, only long-time indebtedness should be classed as a fixed liability. There are no fixed liabilities listed in Mr. Mann's balance sheet.

Proprietorship. As previously explained, accounts representing the proprietorship element may constitute either permanent or temporary proprietorship accounts.

Permanent Proprietorship Accounts. The permanent proprietorship accounts kept in recording the operations of a particular enterprise depend upon the type of legal organization, that is, whether the enterprise is organized as a sole proprietorship, as a partnership, or as a corporation.

In the case of a sole proprietorship, one or more accounts representing the proprietor's interest or equity in the assets may be kept. Reference to Mr. Mann's chart of accounts shown on page 142, will reveal that the following accounts are classified as proprietorship accounts:

Account No. 31, W. L. Mann, Proprietor
Account No. 32, W. L. Mann, Drawing
Account No. 33, Profit and Loss Summary

Account No. 31 reflects the amount of Mr. Mann's proprietorship. It may be increased by additional investments or by failing to withdraw all of his net income from the enterprise; it may be decreased by withdrawals in excess of his net income or by sustaining a net loss during one or more fiscal periods. Usually there will be no changes in the balance of this account during the accounting period, in which case the balance represents the proprietor's investment in the business as of the beginning of the accounting period and until such time as the books are closed at the end of the accounting period.

Account No. 32 is Mr. Mann's drawing account. This account is charged for any withdrawals of cash or other property for personal use. In a sense it is a temporary account in which is kept a record of the proprietor's personal drawings during the accounting period. Such drawings ordinarily are made in anticipation of earnings rather than as a withdrawal of capital. The balance of the account, as shown by the trial balance at the close of an accounting period, represents the total amount of the proprietor's drawings during the period.

Reference to Mr. Mann's work sheet shown on pages 196 and 197 will reveal that the balance of his drawing account is listed in the Dr. column of the Balance Sheet columns. When a drawing account has a debit balance, it is customary to list it in the Dr. column; however, it represents a deduction from proprietorship. The balance is listed in the

Dr. column because there is no provision on a work sheet for making deductions except by listing items in opposite columns. Since the balance of the proprietor's capital account is listed in the Cr. column of the Balance Sheet columns, the listing of the balance of the proprietor's drawing account in the Dr. column is equivalent to deducting it from the balance of the proprietor's capital account.

Account No. 33 is used only at the close of the accounting period for the purpose of summarizing the temporary proprietorship accounts. Sometimes this account is referred to as a *clearing account.* No entries should appear in the account before the books are closed at the end of the accounting period.

Temporary Proprietorship Accounts. As previously explained, the temporary proprietorship accounts include all accounts representing increases or decreases in proprietorship. These accounts are discussed in detail later in this unit.

Interpreting the Balance Sheet. Interpreting the balance sheet involves an analysis of the accounts summarized in it. If an individual desires to know his financial status, a balance sheet will provide the information. It may not be sufficient, however, merely to know how much property one owns or how much one is worth. When the balance sheet is prepared in proper form, it provides information as to the nature and the amount of the property owned, how much of it is in the form of cash or other current assets, how much is invested in fixed assets, what debts are owed, and the amount of the proprietor's net worth or present capital.

A balance sheet as of one date may be compared with a balance sheet as of another date to ascertain the amount of the increase or the decrease in any of the accounts or groups of accounts. Sometimes balance sheets as of two or more dates are prepared in comparative form by listing the amounts as of different dates in parallel columns. Thus, if balance sheets as of the close of two succeeding calendar years are compared, it is possible to ascertain the amount of the increase or the decrease during the intervening period in any of the accounts or groups of accounts listed thereon. If such a comparison reveals an increase in accounts receivable, it may indicate that collections during the later period were not as favorable as they were during the preceding period. If the comparison reveals an increase in accounts payable, it may indicate an inability to pay current bills because of insufficient cash. If the comparison reveals an increase in the current assets without a corresponding increase in the liabilities, it may indicate an improved financial position or status.

Too much emphasis should not be placed upon an increase or a decrease in cash. Some individuals are inclined to judge the results of operations largely by the cash balance. This practice may, however, be misleading. The net results of operations can be properly determined only by comparison of all the assets and the liabilities. The ability of an individual or a firm to meet its current obligations may be determined largely by an analysis of the current assets, particularly those assets that are sometimes referred to as the quick assets. *Quick assets* include cash and all other current assets that are readily convertible into cash, such as marketable securities.

The relation of an account, a group of accounts, or an accounting element to another account, group of accounts, or accounting element may be referred to as the *ratio.* For instance, if the total current assets amount to twice as much as the total current liabilities, the ratio thereof is said to be 2 to 1. Ratios may be expressed in percentages or on a basis of units. Fractions of units may be expressed by means of common fractions or decimals, as for example 7¾ to 1 or 7.75 to 1.

In an enterprise where capital invested is a material income-producing factor, such as is the case in a merchandising enterprise, the ratio of the current assets to the current liabilities may be important. Reference to W. L. Mann's balance sheet shown on pages 206 and 207 reveals that his total current assets amount to $45,306.71 and his total current liabilities amount to $5,557.99, a ratio of better than 8 to 1. His total assets amount to $48,139.76 and his total liabilities amount to $5,557.99, a ratio of nearly 8⅔ to 1. These ratios are sufficiently high to indicate a very favorable financial condition.

Banks often consider the ratio of current assets to current liabilities when considering the advisability of making a loan. It is not expected that an individual or a firm will sell fixed assets to realize sufficient funds with which to pay a short-time loan. If the balance sheet of an individual or a firm seeking a loan does not indicate that a sufficient amount of cash will be realized from the collection of accounts receivable or from the sales of service or merchandise to repay the loan at maturity, the bank may consider the loan inadvisable.

Ratio analysis may be helpful to the prospective investor in evaluating the securities of a corporation, such as bonds and capital stock. Financial writers frequently refer to the ratios of various items in discussing the balance sheets of corporations. This fact will be readily noted in reading financial magazines or the financial pages of newspapers.

The amount invested in current assets as shown by the balance sheet is often said to represent the amount of the *working capital.* The excess of the amount of the current assets over the amount of the current liabilities represents the net working capital.

It is difficult to estimate what the ratio of current assets to current liabilities should be, because of the variations in enterprises and industries. A 2 to 1 ratio of current assets to current liabilities may be more than sufficient in some enterprises but entirely insufficient in others. In the milk business, for example, a 1 to 1 ratio of current assets to current liabilities is considered satisfactory. The reasons are that very little capital is tied up in an inventory, the amount of accounts receivable is comparatively small, and the terms on which the milk is purchased from farmers are such that settlements are slow and comparatively large amounts are due to farmers at all times. Another reason is that a large amount of capital is invested in fixed assets, such as equipment for treating the milk and for delivering it to customers.

Generally speaking, the ratio of the current assets to the current liabilities should be maintained at from 2 to 1 to 5 to 1. While a standard ratio cannot be established for all enterprises, a knowledge of the working capital requirements of a particular enterprise will be helpful in determining what the ratio of current assets to current liabilities should be.

PRACTICE ASSIGNMENT No. 16. Complete Report No. 16 in the workbook and submit your working papers to the instructor for approval. Continue with the following study assignment until Report No. 17 is required.

XVII THE PROFIT AND LOSS STATEMENT

A detailed statement of the increases and the decreases in proprietorship during an accounting period is known as a *profit and loss statement.* The statement should show the sources and amount of income and gains and the nature and amount of costs and expenses of the period.

Function of the Profit and Loss Statement. A profit and loss statement is designed to supplement the information provided by a balance sheet. A balance sheet provides information as to the financial condition at the close of an accounting period, while a profit and loss statement provides information as to the results of the operations during an accounting period.

A profit and loss statement is sometimes referred to as a statement of income and expenses or as an operating statement. In this discussion the designation "profit and loss statement" is used.

A profit and loss statement may be prepared for any individual, unit of organization, or commercial unit. If an individual conducts more than one business and each business is operated independently of the other, a profit and loss statement may be prepared for each business. Both the balance sheet and the profit and loss statement are financial statements in that both provide information with respect to the financial operations of an individual or an enterprise.

Form of the Profit and Loss Statement. A profit and loss statement is usually prepared in narrative or report form. The heading of the statement is similar to the heading of a balance sheet, but there is a difference in dating the statements. The balance sheet represents the financial condition at a specified time, while a profit and loss statement represents the results of operations over a specified period of time. Unless the period of time covered by a profit and loss statement is indicated in the heading, it is impossible to interpret the results.

The body of a profit and loss statement should be arranged with a view to providing, in the most convenient form, the essential information regarding the operations. The information should also be provided in a form that may be readily interpreted. The information that is provided will vary somewhat, depending upon the nature of the operations, the sources of income, the nature of the expenses incurred in earning the income, and whether or not any losses were sustained.

An individual who derives all of his income from compensation should list such compensation in his profit and loss statement as his income, and he should list his expenses and show the total thereof as a deduction from his income. The result will be his net income or his net loss for the period covered by the statement.

An individual who is engaged in business for himself and who derives the major part of his income from sales of products or service should list such income in his profit and loss statement as operating income. From the total operating income should be deducted all costs and operating expenses in order to find the net operating income. To the net operating income should be added any other income and profits, and from this total should be deducted all other charges in order to find the net income or the net loss for the period covered by the statement.

A profit and loss statement may be typed on plain bond paper or may be penwritten on ruled paper. The profit and loss statement of W. L. Mann shown on page 215 is reproduced from penwritten copy.

W. L. Mann

Profit and Loss Statement for Ten Months' Period Ended October 31, 19--

Operating Income:				
Sales			86125	49
Less Sales Returns + Allow.			110	10
Net Sales			86015	39
Less Cost of Sales:				
Mdse. Inventory, beginning of period	28522	45		
Purchases	56495	82		
Total	85018	27		
Less Purchases Ret. + Allow	116	10		
Merchandise available for sale	84902	17		
Less Mdse. Inv.-end of period	32453	96	52448	21
Gross Profit on Sales			33567	18
Operating Expenses:				
Rent Expense	5000	00		
Depreciation Expense	681	95		
Loss on Bad Debts	476	90		
Advertising Expense	4342	12		
Tel. & Tel. Expense	198	40		
Heating & Lighting	494	90		
Stationery & Supplies Consumed	110	00		
Salaries and Commissions	11222	80		
Social Security Taxes	505	03		
Insurance Expense	179	47		
Truck Expense	443	50		
Miscellaneous Expenses	375	93		
Total Operating Expenses			24031	00
Net Operating Income			9536	18
Other Income:				
Interest Income	60	89		
Purchases Discount	181	46		
Total Other Income			242	35
			9778	53
Other Charges:				
Interest Expense	91	76		
Charitable Contributions	145	00		
Total Other Charges			236	76
Net Income			9541	77

Profit and Loss Statement

The information needed in preparing this statement was obtained from the work sheet shown on pages 196 and 197.

The net income shown in the profit and loss statement is the same as the net income shown in the balance sheet.

Classification of Accounts in the Profit and Loss Statement. There are two classes of temporary accounts. Those representing increases in proprietorship consist of income and gains; those representing decreases in proprietorship consist of expenses and losses. Following is a discussion of both classes of accounts:

Income Accounts. Accounts representing income and gains constitute increases in proprietorship. In a mercantile enterprise, the income accounts are usually classified as follows:

(a) Operating income.
(b) Other income.

The operating income is the income derived from the sale of merchandise. The gross profit on sales is computed by subtracting the cost of the merchandise sold from the net sales. Sometimes the cost of sales is not shown in detail in the profit and loss statement, but is shown in a separate statement arranged as follows:

STATEMENT OF COST OF SALES

Merchandise Inventory, beginning of period	$28,522.45
Purchases	56,495.82
Total	$85,018.27
Less Purchases Returns and Allowances	116.10
Cost of Merchandise available for sale	$84,902.17
Less Merchandise Inventory, end of period	32,453.96
Cost of Sales	$52,448.21

The work sheet provides the information needed in computing the cost of sales. Reference to Mr. Mann's work sheet reproduced on pages 196 and 197 will show that the cost of sales account is debited in the Adjustments columns for (a) the inventory at the beginning of the period, $28,522.45, and (b) purchases, $56,495.82, and is credited for (a) the inventory at the end of the period, $32,453.96, and (b) purchases returns and allowances, $116.10. The difference between the sum of the debits and the sum of the credits, amounting to $52,448.21, represents the cost of sales. This amount is extended to the Profit and Loss Dr. column of the work sheet.

Other income should include income or gains derived from any source other than the sale of merchandise, such as interest income, purchases discount, dividends received, and gains derived from the sale of investment property. Reference to Mr. Mann's profit and loss statement will show that his other income consisted of interest income and purchases discount.

Expense Accounts. Accounts representing expenses and losses constitute decreases in proprietorship. In a mercantile enterprise, the expense accounts may be classified as follows:

(a) Operating expenses.
(b) Other charges.

Operating expenses should include all of the ordinary and necessary expenses incurred in operating the business, such as rent expense, depreciation expense, advertising expense, loss on bad debts, salaries, social security taxes, insurance expense, telephone and telegraph expense, heating and lighting expense, stationery and supplies consumed, delivery expense, and any other miscellaneous business expenses.

Other charges should include any expenses incurred or losses sustained that have no relation to the ordinary operations of the enterprise, such as interest expense, charitable contributions, losses on investments, and any other items that cannot properly be classified as operating expenses.

Reference to Mr. Mann's profit and loss statement will reveal that he has a number of operating expenses and other charges, the latter consisting of interest expense and charitable contributions.

Interpreting the Profit and Loss Statement. A profit and loss statement should provide detailed information in regard to the following:

(a) The sources of the income and the amount of income derived from each source.
(b) The nature of the expenses and the amount of each kind of expense.
(c) The net income or the net loss for the accounting period.

The information that a profit and loss statement provides should be of value to the proprietor or the management of the enterprise when it is used as a basis for planning the future operations.

If desired, an analysis may be made of the important items. When the various items are analyzed in this manner, the principal source of income is usually considered as the base, or 100 per cent.

Mr. Mann's profit and loss statement shows that his net sales amounted to $86,015.39. Treating this sum at 100 per cent, his cost of sales amounting to $52,448.21 was equal to 60.98 per cent of his net sales; his operating expenses, amounting to $24,031, were equal to 27.9 per cent of his net sales; his net income, amounting to $9,541.77, was equal to 11.09 per cent of his net sales. It may be of value to make a similar percentage analysis of the various items on the profit and loss statements for succeeding accounting periods in order to ascertain the trend.

By analyzing the balance sheet and the profit and loss statement together, additional information may be obtained, such as the relation of the net income to the amount of capital invested in the enterprise.

During the ten-months' period ended October 31, Mr. Mann's net income amounted to approximately 26.5 per cent of his capital investment ($9,541.77 ÷ $36,000). It is important to note, however, that the net income of $9,541.77 was computed without any deduction for salary or drawings of Mr. Mann during the period.

Turnover. A merchant is usually interested also in ascertaining the rate of *turnover* for each accounting period. This has reference to the number of times the merchandise available for sale is turned during the accounting period. The rate of turnover is ascertained by dividing the cost of sales for the period by the average inventory. Where an inventory is taken only at the end of each accounting period, the average inventory for the period may be ascertained by adding the beginning and ending inventories together and dividing by two. Mr. Mann's turnover for the ten-months' period ended October 31 may be computed as follows:

Beginning inventory	$28,522.45
Ending inventory	32,453.96
Cost of sales for the period	52,448.21

$28,522.45 + $32,453.96 ÷ 2 = $30,488.21
$52,448.21 ÷ $30,488.21 = 1.7

This indicates a turnover of approximately 1⅔ times the average inventory for the ten-months' period, which is equivalent to a turnover of two times the average inventory for the full year. In the retail furniture business, a turnover of from 2½ to 3 times the average inventory is considered normal. It is evident, therefore, that Mr. Mann's rate of turnover is a little below normal. A careful analysis of the theory involved in computing the rate of turnover will indicate that the greater the turnover the smaller the profit need be on each dollar of sales in order to produce a satisfactory gross profit on sales.

PRACTICE ASSIGNMENT No. 17. *Complete Report No. 17 in the workbook and submit your working papers to the instructor for approval. After completing the report, you may continue with the textbook discussion in Unit Eight until the next report is required.*

Unit Eight

ADJUSTING AND CLOSING ACCOUNTS

XVIII ADJUSTING ENTRIES

As explained in the preceding unit, adjustment of certain accounts may be required because of changes that have occurred during the period but which are not reflected in the accounts. Thus in preparing the work sheet for Mr. Mann, which is reproduced on pages 196 and 197, certain adjustments were made for the following purposes:

(a) To transfer the amount of the merchandise inventory at the beginning of the accounting period to the cost of sales account.

(b) To record the amount of the merchandise inventory taken at the end of the accounting period.

(c) To transfer the balance of the purchases account to the cost of sales account.

(d) To transfer the balance of the purchases returns and allowances account to the cost of sales account.

(e) To record the amount of the interest accrued on notes receivable.

(f) To record the amount of the interest accrued on notes payable.

(g) To record the amount of the insurance expired during the period.

(h) To record the amount of the stationery and supplies consumed during the period.

(i) To record the amount of the depreciation of fixed assets estimated to have been sustained during the period.

(j) To record the amount added to the reserve for bad debts.

The effect of these adjustments was reflected in the financial statements. To bring the ledger into agreement with the financial statements, the amounts of the adjustments should be recorded in the proper accounts. It is customary, therefore, at the end of each accounting period to journalize the adjustments and to post to the accounts affected.

Journalizing the Adjusting Entries. The adjusting entries may be recorded either in a general journal or in a combined cash-journal. The information needed in journalizing the adjusting entries may be obtained from the Adjustments columns of the work sheet. Assuming that the accounts of Mr. Mann are to be adjusted at the close of the period ending October 31, the required entries arranged in general journal form are as follows:

Adjusting Entries

Oct. 31.	Cost of Sales	$28,522.45	
	Merchandise Inventory		$28,522.45
	Beginning inventory transferred to Cost of Sales.		
31.	Merchandise Inventory	32,453.96	
	Cost of Sales		32,453.96
	Ending inventory recorded.		
31.	Cost of Sales	56,495.82	
	Purchases		56,495.82
	Purchases transferred to Cost of Sales.		
31.	Purchases Returns and Allowances	116.10	
	Cost of Sales		116.10
	Purchases returns and allowances transferred to Cost of Sales.		
31.	Accrued Interest Receivable	18.70	
	Interest Income		18.70
	Interest accrued on notes receivable.		
31.	Interest Expense	40.56	
	Accrued Interest Payable		40.56
	Interest accrued on notes payable.		
31.	Insurance Expense	179.47	
	Prepaid Insurance		179.47
	Insurance expired during period.		
31.	Stationery and Supplies Consumed	110.00	
	Stationery and Supplies		110.00
	Stationery and supplies consumed during period.		
31.	Depreciation Expense	154.17	
	Reserve for Depreciation of Store Equipment		154.17
	Depreciation sustained at 10% for 10 months.		
31.	Depreciation Expense	527.78	
	Reserve for Depreciation of Delivery Equipment		527.78
	Depreciation sustained at 33⅓% for 10 months.		
31.	Loss on Bad Debts	476.90	
	Reserve for Bad Debts		476.90
	Increase reserye for bad debts, 1% of charge sales.		

COMBINED CASH-JOURNAL

DATE MO.	DATE DAY	DESCRIPTION	POST. REF.	GENERAL DEBITS	GENERAL CREDITS
		AMOUNTS FORWARDED			
19– Oct.	31	Adjusting Entries:			
		Cost of Sales-Mdse. Inventory	52/14	28 522 45	28 522 45
		Mdse. Inventory-Cost of Sales	14/52	32 453 96	32 453 96
		Cost of Sales-Purchases	52/51	56 495 82	56 495 82
		Purchases R & A - Cost of Sales	051/52	116 10	116 10
		Accr. Int. Rec.-Interest Income	15/421	18 70	18 70
		Interest Expense-Accr. Int. Pay.	631/25	40 56	40 56
		Ins. Expense-Prepaid Ins.	620/16	179 47	179 47
		Sta. & Sup. Cons.-Sta. & Supplies	619/17	110 00	110 00
		Depr. Expense-Res. for Depr. S. E.	612/018	154 17	154 17
		Depr. Expense-Res. for Depr. D. E.	612/019	527 78	527 78
		Loss on Bad Debts-Res. for Bad Debts.	613/012	476 90	476 90
				119 095 91	119 095 91

Adjusting Entries for a Mercantile Enterprise

The procedure in recording the adjusting entries in Mr. Mann's combined cash-journal is shown in the above illustration in which a section of his combined cash-journal is reproduced. It will be observed that the titles of the accounts to be debited and credited are entered in the Description column and the amounts are entered in the General Dr. and Cr. columns. A comparison of the combined cash-journal entries with the foregoing general journal entries will reveal that the results will be the same when the posting is completed from either journal.

Posting the Adjusting Entries. The adjusting entries should be posted individually to the proper general ledger accounts. The accounts of Mr. Mann that were affected by the adjusting entries are reproduced on the following pages. The entries for transactions made prior to posting the adjusting entries are the same as appeared in the corresponding accounts in Mr. Mann's general ledger reproduced on pages 180 to 184. In posting the adjusting entries, it is advisable to write a brief description of each entry in the Items column of the accounts. For example, in posting the adjusting entry to transfer the beginning inventory to the cost of sales account, the description "Beginning inventory" was written in the Items

(Continued on page 224)

Reserve for Bad Debts — Account No. 012

				19--			
				Oct. 1	Balance	√	88.56
				31	1% of charge sales	CJ221	476.90
							565.46

Merchandise Inventory — Account No. 14

19--				19--			
Oct. 1	Balance	√	28,522.45	Oct. 31	Cost of Sales	CJ221	28,522.45
31	Inventory	CJ221	32,453.96				

Accrued Interest Receivable — Account No. 15

19--							
Oct. 31	Accrued	CJ221	18.70				

Prepaid Insurance — Account No. 16

19--				19--			
Oct. 1	Balance	√	430.72	Oct. 31	Expired	CJ221	179.47
	251.25						

Stationery and Supplies — Account No. 17

19--				19--			
Oct. 1	Balance	√	155.00	Oct. 31	Consumed	CJ221	110.00
31		CJ177	15.00				
	60.00		*170.00*				

Reserve for Depreciation of Store Equipment — Account No. 018

				19--			
				Oct. 1	Balance	√	370.00
				31	Depr. 10%	CJ221	154.17
							524.17

Reserve for Depreciation of Delivery Equipment — Account No. 019

				19--			
				Oct. 1	Balance	√	475.00
				31	Depr. 33⅓%	CJ221	527.78
							1,002.78

Accrued Interest Payable — Account No. 25

				19--			
				Oct. 31	Accrued	CJ221	40.56

Interest Income — Account No. 421

				19--			
				Oct. 1	Balance	√	42.19
				31	Accrued interest	CJ221	18.70
							60.89

PURCHASES Account No. 51

19--				19--			
Oct. 1	Balance	√	54,450.17	Oct. 31	Cost of sales	CJ221	56,495.82
31		P178	2,045.65				
			56,495.82				
			56,495.82				56,495.82

PURCHASES RETURNS AND ALLOWANCES Account No. 051

19--				19--			
Oct. 31	Cost of Sales	CJ221	116.10	Oct. 1	Balance	√	72.00
				20		CJ177	24.80
				28		CJ177	19.30
							116.10
			116.10				116.10

COST OF SALES Account No. 52

19--				19--			
Oct. 31	Beg. inventory	CJ221	28,522.45	Oct. 31	End. inventory	CJ221	32,453.96
31	Purchases	CJ221	56,495.82	31	Pur. R. & A.	CJ221	116.10
	52,448.21		*85,018.27*				*32,570.06*

DEPRECIATION EXPENSE Account No. 612

19--							
Oct. 31	Store Equip.	CJ221	154.17				
31	Del. Equip.	CJ221	527.78				
			681.95				

LOSS ON BAD DEBTS Account No. 613

19--							
Oct. 31	1% of charge sales	CJ221	476.90				

STATIONERY AND SUPPLIES CONSUMED Account No. 617

19--							
Oct. 31	Consumed	CJ221	110.00				

INSURANCE EXPENSE Account No. 620

19--							
Oct. 31	Expired	CJ221	179.47				

INTEREST EXPENSE Account No. 631

19--							
Oct. 1	Balance	√	51.20				
31	Accrued interest	CJ221	40.56				
			91.76				

column on the debit side of the cost of sales account and the description "Cost of Sales" was written in the Items column on the credit side of the merchandise inventory account. As each adjusting entry was posted, similar descriptive information was entered in the Items column of the accounts affected.

The pages of the combined cash-journal from which the adjusting entries were posted were entered in the Folio columns of the general ledger as the posting was completed. The account numbers were also entered in the Posting Reference column of the combined cash-journal as the posting was completed. This provided a suitable cross reference in both books of account.

Cost of Sales Account. The cost of sales account is a summary account that is used only at the close of an accounting period. After posting the adjusting entries, the balance of the cost of sales account represents the cost of merchandise sold during the period. This balance is the same as the cost of sales shown in the work sheet reproduced on pages 196 and 197, and in the profit and loss statement reproduced on page 215.

Ruling the Merchandise Inventory Account. After posting the adjusting entry required to transfer the beginning inventory to the cost of sales account, the merchandise inventory account was in balance. It was ruled as shown on page 222. When one item only is recorded on each side of an account, it may be ruled by drawing a single line across the amount columns. In posting the entry to record the inventory taken at the end of the period, the debit to the merchandise inventory account was recorded on the next horizontal line below the rule.

Ruling the Purchases Account. After posting the entry required to transfer the net purchases for the period to the cost of sales account, the purchases account was in balance. It was ruled as shown on page 223. When more than one item is recorded on either side of an account, the ruling should be completed by drawing a single line across the amount columns only and, after entering the totals on the next horizontal line, by ruling double lines across all the columns except the Items columns. When accounts are ruled in this manner, the single rule denotes addition and the double rule denotes balancing or closing.

PRACTICE ASSIGNMENT No. 18. Complete Report No. 18 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 19 is required.

XIX CLOSING ENTRIES

After the adjusting entries are posted at the end of the accounting period, the temporary proprietorship accounts should be closed by transferring their balances to the profit and loss summary account. This process may be referred to as (a) closing the books, (b) closing the ledger, or (c) closing the temporary proprietorship accounts. It is customary to journalize the closing entries. They may be recorded either in a general journal or a combined cash-journal. If they are recorded in a general journal, a separate entry may be made to close each account. Much time may be saved, however, by combining the accounts into two groups and closing each group by means of a compound journal entry.

Journalizing the Closing Entries. The information needed in journalizing the closing entries may be obtained from the Profit and Loss columns of the work sheet. By referring to W. L. Mann's work sheet reproduced on pages 196 and 197, it will be noted, under the heading Profit and Loss, that the accounts with debit balances are listed in the left-hand column and the accounts with credit balances are listed in the right-hand column.

Temporary accounts with credit balances represent increases in proprietorship. To close these accounts their balances must be transferred to the profit and loss summary account; thus accounts with credit balances are closed by debiting such accounts and by crediting Profit and Loss Summary.

Temporary accounts with debit balances, including the cost of sales, sales returns and allowances, and expense accounts, represent decreases in proprietorship. To close these accounts their balances must be transferred to the profit and loss summary account; thus accounts with debit balances may be closed by crediting such accounts and by debiting Profit and Loss Summary.

The general journal entries required to close W. L. Mann's temporary proprietorship accounts follow.

CLOSING ENTRIES

Oct. 31.	Sales	$86,125.49	
	Interest Income	60.89	
	Purchases Discount	181.46	
	Profit and Loss Summary		$86,367.84
	Closing the income accounts into the profit and loss summary account.		

Oct. 31. Profit and Loss Summary	$76,826.07	
Cost of Sales		$52,448.21
Sales Returns and Allowances		110.10
Rent Expense		5,000.00
Depreciation Expense		681.95
Loss on Bad Debts		476.90
Advertising Expense		4,342.12
Telephone and Telegraph Expense		198.40
Heating and Lighting		494.90
Stationery and Supplies Consumed		110.00
Salaries and Commissions		11,222.80
Social Security Taxes		505.03
Insurance Expense		179.47
Truck Expense		443.50
Miscellaneous Expenses		375.93
Interest Expense		91.76
Charitable Contributions		145.00
Closing the cost of sales, sales returns and allowances, and expense accounts into the profit and loss summary account.		

The next step is to draft a journal entry to close the profit and loss summary account. W. L. Mann's net income for the ten-months' period ended October 31 amounted to $9,541.77. His net income was first ascertained by preparing a work sheet, and the amount was subsequently confirmed by preparing a profit and loss statement. Reference to Mr. Mann's drawing account reproduced on page 182 will show that during the period he withdrew a total of $2,960 for personal use. A sufficient amount of the net income should be transferred to his drawing account to balance it. Assuming that he wishes the remainder of the net income transferred to his capital account, the profit and loss summary account may be closed by means of the following general journal entry:

Oct. 31. Profit and Loss Summary	$9,541.77	
W. L. Mann, Drawing		$2,960.00
W. L. Mann, Proprietor		6,581.77
Closing the profit and loss summary account.		

The procedure in recording the closing entries in Mr. Mann's combined cash-journal is shown in the following illustration, in which a section of his combined cash-journal is reproduced. It will be observed that the titles of the accounts to be debited and credited are entered in the Description column and the amounts are entered in the General Dr. and Cr. columns. A comparison of the combined cash-journal entries with the foregoing general journal entries will reveal that the results will be the same when the posting is completed from either journal.

COMBINED CASH-JOURNAL

DATE MO.	DATE DAY	DESCRIPTION	POST. REF.	GENERAL DEBITS	GENERAL CREDITS
		AMOUNTS FORWARDED			
19— Oct.	31	Closing Entries:			
		Sales—P.&L. Summary	411/33	86125 49	86125 49
		Interest Income—"	421/33	60 89	60 89
		Purchases Discount—"	422/33	181 46	181 46
		P&L Summary—Cost of Sales	33/52	52448 21	52448 21
		" —Sales R. & A.	33/041	110 10	110 10
		" —Rent Expense	33/611	5000 00	5000 00
		" —Depr. Expense	33/612	681 95	681 95
		" —Loss on Bad Debts	33/613	476 90	476 90
		" —Adv. Expense	33/614	4342 12	4342 12
		" —T&T Expense	33/615	198 40	198 40
		" —Heating & Lighting	33/616	494 90	494 90
		" —Sta. & Sup. Consumed	33/617	110 00	110 00
		" —Sal. & Com.	33/618	11222 80	11222 80
		" —S. S. Taxes	33/619	505 03	505 03
		" —Ins. Expense	33/620	179 47	179 47
		" —Truck Expense	33/621	443 50	443 50
		" —Misc. Expenses	33/622	375 93	375 93
		" —Int. Expense	33/631	91 76	91 76
		" —Char. Contributions	33/632	145 00	145 00
		" —W. L. Mann, Drawing	33/32	2960 00	2960 00
		" —W. L. Mann, Prop.	33/31	6581 77	6581 77
				172735 68	172735 68

Closing Entries for a Mercantile Enterprise

Posting the Closing Entries. The closing entries should be posted individually to the proper general ledger accounts. The accounts of Mr. Mann that were affected by the closing entries are reproduced on pages 229 to 233. In posting the closing entries, it is advisable to write a brief description of each entry in the Items column of the accounts. For example, in posting the entry required to close the sales account, the description "P. & L." was written in the Items column on the debit side of the sales account and the description "Sales" was written in the Items column on the credit side of the profit and loss summary account. As each closing entry was posted, similar descriptive information was entered in the Items column of the accounts affected. When this is done, the identity of each account closed into the profit and loss summary account is indicated.

The page of the combined cash-journal from which the closing entries were posted was entered in the Folio column of the general ledger as the posting was completed. The account numbers were also entered in the Posting Reference column of the combined cash-journal as the posting was completed. This provided a suitable cross reference in both books of account.

Balancing and Ruling Accounts. Accounts that are in balance after the adjusting and closing entries have been posted at the close of the accounting period should be ruled. It will be noted that all of Mr. Mann's temporary accounts were ruled after posting the adjusting and closing entries. In addition to the temporary proprietorship accounts that are closed and ruled at the end of each accounting period, certain other accounts may be balanced and ruled. For example, it is customary to balance and rule the proprietor's capital account. The procedure in balancing and ruling Mr. Mann's capital account was as follows:

(a) Footed the credit amount column and recorded the footing in small pencil figures just below the line on which the last entry appeared.

(b) The balance of the account represented Mr. Mann's present capital. Recorded the balance on the debit side of the account in order to balance it.

(c) Ruled a single line across both the Dr. and Cr. amount columns to denote addition and recorded the totals on the next horizontal line below the rules.

(d) Ruled a double line just below the totals across all columns except the Items columns.

(e) Brought the balance down below the ruling on the credit side of the account.

After it was balanced and ruled on October 31, Mr. Mann's capital account appeared as shown on page 229.

It is also customary to balance and rule the bank checking account at the end of each accounting period. After it was balanced and ruled on October 31, Mr. Mann's bank checking account appeared as shown on page 229.

(Continued on page 233)

ACCOUNT *Liberty National Bank* ACCOUNT No. 111

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		8249.04	19– Oct.	31		CJ177		4899.63
	31	7271.22	CJ177		3921.81		31	Balance	✓		7271.22
					12170.85						12170.85
Nov.	1	Balance	✓		7271.22						

ACCOUNT *W. L. Mann, Proprietor* ACCOUNT No. 31

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	31	Balance	✓		42581.77	19– Oct.	1	Balance	✓		36000.00
							31	P.&L.	CJ227		6581.77
					42581.77						42581.77
						Nov.	1	Balance	✓		42581.77

ACCOUNT *W. L. Mann, Drawing* ACCOUNT No. 32

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	1	Balance	✓		2700.00	19– Oct.	31	P.&L.	CJ227		2960.00
	21		CJ177		250.00						
	31		CJ177		10.00						
					2960.00						2960.00

ACCOUNT *Profit and Loss Summary* ACCOUNT No. 33

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19– Oct.	31	Cost of Sales	CJ227		52448.21	19– Oct.	31	Sales	CJ227		86125.49
	31	Sales R.&A.	CJ227		110.10		31	Int. Income	CJ227		60.89
	31	Rent Expense	CJ227		5000.00		31	Pur. Discount	CJ227		181.46
	31	Depr. Expense	CJ227		681.95						
	31	Loss on Bad Debts	CJ227		476.90						
	31	Adv. Expense	CJ227		4342.12						
	31	T.&T. Expense	CJ227		198.40						
	31	Heat & Light	CJ227		494.90						
	31	Sta. & Supplies	CJ227		110.00						
	31	Sal. & Com.	CJ227		1122.80						
	31	S.S. Taxes	CJ227		505.03						
	31	Ins. Expense	CJ227		179.47						
	31	Truck Expense	CJ227		443.50						
	31	Misc. Expenses	CJ227		375.93						
	31	Int. Expense	CJ227		91.76						
	31	Char. Contrib.	CJ227		145.00						
	31	W.L. Mann, Draw.	CJ227		2960.00						
	31	W.L. Mann, Prop.	CJ227		6581.77						
					86367.84						86367.84

ACCOUNT *Sales* ACCOUNT No. 411

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31	P & L	CJ227		86125 49	19— Oct.	1	Balance	✓		81604 40
							7		CJ176		320 00
							14		CJ176		465 00
							21		CJ177		379 94
							28		CJ177		549 37
							31		CJ177		194 40
							31		S178		2612 38
											86125 49
					86125 49						86125 49

ACCOUNT *Sales Returns and Allowances* ACCOUNT No. 0411

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		90 00	19— Oct.	31	P & L	CJ227		110 10
	12		CJ176		9 10						
	27		CJ177		11 00						
					110 10						
					110 10						110 10

ACCOUNT *Interest Income* ACCOUNT No. 421

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31	P & L	CJ227		60 89	19— Oct.	1	Balance	✓		42 19
							31	Accru interest	CJ221		18 70
											60 89
					60 89						60 89

ACCOUNT *Purchases Discount* ACCOUNT No. 422

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31	P & L	CJ227		181 46	19— Oct.	1	Balance	✓		176 50
							23		CJ177		4 96
											181 46
					181 46						181 46

ACCOUNT *Cost of Sales* ACCOUNT No. 52

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31	Beg inventory	CJ221		28522 45	19— Oct.	31	End inventory	CJ221		32453 96
	31	Purchases 52448 21	CJ221		56495 82		31	Pur R & A	CJ221		116 10
					85018 27						32570 06
							31	P & L	CJ227		52448 21
											85018 27
					85018 27						85018 27

ACCOUNT *Rent Expense* ACCOUNT No. 611

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		4500 00	19— Oct.	31	P & L	CJ227		5000 00
	2		CJ176		500 00						
					5000 00						
					5000 00						5000 00

ACCOUNT *Depreciation Expense* ACCOUNT No. 612

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct	31	Store Equip.	CJ221		154 17	19— Oct.	31	P.&L.	CJ227		681 95
	31	Del. Equip.	CJ221		527 78						
					681 95						681 95

ACCOUNT *Loss on Bad Debts* ACCOUNT No. 613

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31	1% of chg. sales	CJ221		476 90	19— Oct.	31	P.&L.	CJ227		476 90

ACCOUNT *Advertising Expense* ACCOUNT No. 614

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		4111 75	19— Oct.	31	P.&L.	CJ227		4342 12
	6		CJ176		53 37						
	27		CJ177		170 00						
	31		CJ177		7 00						
					4342 12						4342 12

ACCOUNT *Telephone and Telegraph Expense* ACCOUNT No. 615

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		180 00	19— Oct.	31	P.&L.	CJ227		198 40
	9		CJ176		17 50						
	31		CJ177		90						
					198 40						198 40

ACCOUNT *Heating and Lighting* ACCOUNT No. 616

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		450 00	19— Oct.	31	P.&L.	CJ227		494 90
	9		CJ176		44 90						
					494 90						494 90

ACCOUNT *Stationery and Supplies Consumed* ACCOUNT No. 617

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	31	Consumed	CJ221		110 00	19— Oct.	31	P.&L.	CJ227		110 00

ACCOUNT *Salaries and Commissions* ACCOUNT No. 618

Date		Items	Folio	✓	Debits	Date		Items	Folio	✓	Credits
19— Oct.	1	Balance	✓		10107 80	19— Oct.	31	P&L	CJ227		11222 80
	14		CJ176		535 00						
	31		CJ177		580 00						
					11222 80						11222 80

ACCOUNT *Social Security Taxes* ACCOUNT No. 619

Date		Items	Folio	✓	Debits	Date		Items	Folio	✓	Credits
19— Oct.	1	Balance	✓		454 85	Oct.	31	P&L	CJ227		505 03
	14		CJ176		24 08						
	31		CJ177		26 10						
					505 03						505 03

ACCOUNT *Insurance Expense* ACCOUNT No. 620

Date		Items	Folio	✓	Debits	Date		Items	Folio	✓	Credits
19— Oct.	31	Expired	CJ221		179 47	19— Oct.	31	P&L	CJ227		179 47

ACCOUNT *Truck Expense* ACCOUNT No. 621

Date		Items	Folio	✓	Debits	Date		Items	Folio	✓	Credits
19— Oct.	1	Balance	✓		385 00	19— Oct.	31	P&L	CJ227		443 50
	2		CJ176		58 50						
					443 50						443 50

ACCOUNT *Miscellaneous Expenses* ACCOUNT No. 622

Date		Items	Folio	✓	Debits	Date		Items	Folio	✓	Credits
19— Oct.	1	Balance	✓		369 78	19— Oct.	31	P&L	CJ227		375 93
	31		CJ177		6 15						
					375 93						375 93

ACCOUNT *Interest Expense* ACCOUNT No. 631

Date		Items	Folio	✓	Debits	Date		Items	Folio	✓	Credits
19— Oct.	1	Balance	✓		51 20	19— Oct.	31	P&L	CJ227		91 76
	31	Accr. interest	CJ221		40 56						
					91 76						91 76

ACCOUNT *Charitable Contributions* ACCOUNT No. 632

DATE		ITEMS	FOLIO	✓	DEBITS	DATE		ITEMS	FOLIO	✓	CREDITS
19— Oct.	1	Balance	✓		140 00	19— Oct.	31	P&L	CJ117		145 00
	31		CJ77		5 00						
					145 00						145 00

Many bookkeepers prefer to use red ink as follows:

(a) In ruling horizontal single and double lines in all books of account.

(b) In balancing accounts whether the balance is to be brought down below the double rule on the same page or is to be carried forward to the top of a new page.

To transfer an account from one page to another, it is customary (a) to foot the account, (b) to ascertain the balance, (c) to record the balance on the next horizontal line on the side which has the lesser footing, (d) to record the totals of both amount columns, and (e) to record the balance on the proper side of the newly opened account, which usually will be the top of a new page in the ledger. The term *Carried Forward* should be written on the line with the balance in the old account and the term *Brought Forward* on the line with the balance in the new account.

Trial Balance After Closing. A trial balance of the open accounts in the general ledger after the temporary proprietorship accounts have been closed is usually referred to as a *post-closing trial balance.* The purpose of this post-closing trial balance is to prove that the general ledger is in balance at the beginning of a new accounting period. Obviously, it is advisable to ascertain that the ledger is in balance before any transactions for the new accounting period are recorded.

The post-closing trial balance should contain the same accounts and amounts as appear in the Balance Sheet columns of the work sheet, except that (a) the proprietor's drawing account is omitted because it has been closed, and (b) the proprietor's capital account has been adjusted for the amount of the net income transferred to it.

A post-closing trial balance of W. L. Mann's accounts is shown on page 234. Some accountants advocate that the post-closing trial balance should be dated as of the close of the old accounting period, while others advocate that it should be dated as of the beginning of the new accounting period. In this illustration the trial balance is dated as of October 31, the closing date of the accounting period.

W. L. MANN

POST-CLOSING TRIAL BALANCE, OCTOBER 31, 19--

Liberty National Bank	$ 7,271.22	
Petty Cash Fund	100.00	
Notes Receivable	801.50	
Accounts Receivable	4,915.54	
Reserve for Bad Debts		$ 565.46
Merchandise Inventory	32,453.96	
Accrued Interest Receivable	18.70	
Prepaid Insurance	251.25	
Stationery and Supplies	60.00	
Store Equipment	2,460.00	
Res. for Depr. of Store Equipment		524.17
Delivery Equipment	1,900.00	
Res. for Depr. of Delivery Equipment		1,002.78
Notes Payable		2,000.00
Accounts Payable		3,329.60
Employees' Income Taxes Payable		90.60
Social Security Taxes Payable		97.23
Accrued Interest Payable		40.56
W. L. Mann, Proprietor		42,581.77
	$50,232.17	$50,232.17

W. L. Mann's Post-Closing Trial Balance

The Accounting Cycle. This unit completes an accounting cycle. The term *accounting cycle* refers to the steps involved in recording the effect of all the transactions completed during an accounting period, beginning with the entries in the books of original entry and ending with the post-closing trial balance. The following is a brief outline of the various steps involved in an accounting cycle, all of which have now been developed:

(1) Journalizing the transactions.

(2) Posting to the ledger accounts.

(3) Taking a trial balance.

(4) Preparing a work sheet.

(5) Preparing a balance sheet and a profit and loss statement.

(6) Journalizing and posting the adjusting and closing entries.

(7) Taking a post-closing trial balance.

PRACTICE ASSIGNMENT No. 19. Complete Report No. 19 in the workbook and submit your working papers to the instructor for approval. After completing the report you may continue with the textbook discussion in Unit Nine until the next report is required.

Unit Nine

THE PERSONAL SERVICE ENTERPRISE

XX ACCOUNTING METHODS

A personal service enterprise is one in which the principal source of income is compensation for personal services rendered. There are two types of personal service enterprises as follows:

(a) Professional enterprises.

(b) Business enterprises.

Professional enterprises include law, medicine, surgery, dentistry, public accounting, engineering, architecture, art, sculpture, and education. The principal source of income of individuals engaged in such professions is usually the compensation received in payment of the personal services rendered.

Business enterprises of the personal service type include real estate, insurance, advertising, transportation, storage, entertainment, brokerage, and many other enterprises in which the income is derived chiefly from personal services rendered. Mercantile enterprises are not classified as personal service enterprises for the reason that their principal source of income is from the sale of merchandise rather than from compensation received for services rendered.

The federal income tax law and other federal and state laws permit each taxpayer to adopt such forms and systems of accounting as are in his judgment best suited to his purpose. However, he is required by law to make an annual return of his true income and he should maintain accounting records that will enable him to do so. Net income may be computed on either of the following bases:

(a) Accrual basis.

(b) Cash receipts and disbursements basis, commonly known as the cash basis.

Individuals engaged in personal service enterprises, whether of a professional or business nature, may keep their accounts on either the accrual basis or the cash basis.

Accounting on the Accrual Basis. The U. S. Supreme Court has held that keeping accounts on the accrual basis means that it is the right to receive, and not the actual receipt, that determines the inclusion of an amount in gross income. When the right to receive income becomes fixed, the right accrues.

The basic idea underlying the accrual system is that the accounts shall reflect income definitely earned, regardless of whether payment is due, and expenses definitely incurred, regardless of whether payment has been made. Thus an advertising agent who elects to keep his accounts on the accrual basis must record income in the period in which it accrues or is earned regardless of when payment is actually received; to be consistent, his expenses must also be recorded in the period in which they accrue regardless of when payment is actually made.

Where it is necessary to use an inventory, only the accrual method will correctly reflect income with respect to purchases and sales. Merchants therefore uniformly keep their accounts on the accrual basis. Sales are recorded as income at the time the merchandise is sold, regardless of when payment is received. Merchandise sold for cash is recorded by debiting Cash and by crediting Sales. When merchandise is sold on credit, the transaction is recorded by debiting Accounts Receivable and by crediting Sales. At the close of the accounting period the balance of the accounts receivable account is listed in the balance sheet as an asset, while the balance of the sales account is listed in the profit and loss statement as income earned during the period.

When the accounts are kept on the accrual basis, it is necessary at the close of the accounting period to adjust certain accounts for accruals and deferred items. Any interest accrued on notes receivable should be recorded as income. Any interest accrued on notes payable should be recorded as an expense. Income collected but not earned during the accounting period should be deferred to the succeeding period in which it is earned. Supplies purchased but not consumed during the accounting period should be deferred to the succeeding period in which they are consumed.

A method of accounting cannot be regarded as clearly reflecting income unless all income and all deductions are treated with reasonable consistency. Thus, if the accounts are kept on the accrual basis, all income should be recorded in the period in which it is earned and all expenses should be recorded in the period in which they are incurred. If this plan is followed consistently, the accounts will reflect the true net income for each accounting period.

Accounting on the Cash Basis. When the accounts are kept on the cash basis, income is based on amounts actually or constructively received and expenses are based on amounts actually expended. Usually the income will be received in cash; however it may be received in some form of property other than cash. Any property received in lieu of cash in payment of services rendered is income to the extent of its fair market value at the time it is received.

Income is constructively received when it is credited to a person's account or is set apart so that he may draw upon it. For example, when interest on a savings account is credited to the depositor's account, such interest is income to the depositor even though it is not actually received in cash or is not immediately withdrawn. When a bond interest coupon matures, the amount represents income to the owner of the bond for the period in which the coupon matures even though it may not be cashed until a later period. Should the interest coupon be exchanged for property other than cash, it is income nevertheless.

While, under the cash basis of accounting, expenses are based on amounts actually expended, they need not be paid in cash. If expenses are paid with property or something other than cash, the amount entailed is the fair market value of the property or other consideration transferred. For example, if a tenant, who is a public accountant, makes an audit of his landlord's accounts in payment of one month's office rent, the amount to be charged to Rent Expense is the fair market value of the services rendered. Thus, if the rental amounts to $100 a month, the fair market value of the services rendered is $100.

The cash basis of accounting is popular with individuals engaged in personal service enterprises for various reasons such as the following:

(a) Income taxes are not imposed on the income before it is actually received in cash.

(b) It is a simple method of accounting; no adjustments for accruals and deferred items are required at the close of the accounting period.

(c) With respect to lawyers, physicians, and dentists, net income is more correctly determinable on the cash basis, for the reason that charges made for services do not constitute binding accounts receivable until such charges have been assented to by their clients or patients.

Application of Principles. As an aid in applying the principles involved in keeping the accounts of a personal service enterprise on the cash basis, a system of accounts for J. C. Allen, an attorney at law, will be described. While certain distinctive problems may arise in keeping the accounts of any specific enterprise, it will be found that the general principles are the same in all cases; hence the system of accounts used by Mr. Allen may readily be adapted to the needs of any personal service enterprise regardless of whether it is of a professional or a business nature.

Chart of Accounts. Mr. Allen's chart of accounts is reproduced on the following page. Reference to this chart will show that each account is given a number as well as an appropriate title. All account numbers beginning with 1 represent assets; 2, liabilities; 3, proprietorship; 4, income; and 5, expenses. Account numbers beginning with 0 represent *valuation accounts* in which it is customary to record the estimated decrease in the value of certain assets caused by depreciation or other factors. This system of numbering accounts permits adding new accounts as they are needed without disturbing the numerical order of the accounts. For example, accounts may be added under the heading of Investment Expenses as needed to record real property expenses such as taxes, insurance, and depreciation. Some of Mr. Allen's accounts are peculiar to the legal profession. Following is a discussion of these accounts and certain other accounts that have not previously been introduced.

Advances in Behalf of Clients, Account No. 14. In handling a legal case, a lawyer may incur certain costs and expenses in behalf of his client. The bar associations consider it unethical for lawyers to stand or absorb such expenses personally. While it is not considered unethical for a lawyer to take a case on a *contingent fee* basis, it is considered unethical for him to incur expenses contingently in behalf of his client. Expenses of this type may include court filing fees, the cost of obtaining depositions, fees charged by accountants employed to make audits, and other similar expenses incurred in behalf of a client in handling his case. When a lawyer incurs expenses in behalf of a client, he usually charges such expenses to an account with Advances in Behalf of Clients. At the same time a record of the charges is made in the client's account on a case docket as will be explained later.

Advances in Behalf of Clients is an asset account. It should be debited for any expenses incurred in behalf of clients and should be credited for remittances received from clients in settlement of such charges. After all posting is completed, the balance of the account represents the aggregate amount due from clients on account of advances made in their behalf.

CHART OF ACCOUNTS FOR J. C. ALLEN, ATTORNEY AT LAW

Note: Items in italics represent headings and not account titles.

I *Assets*
- *11 Cash in Bank*
  - 111 First National Bank — Checking
  - 112 First National Bank — Savings
- 12 Petty Cash Fund
- 13 Notes Receivable
- 14 Advances in Behalf of Clients
- *15 Investments*
  - 151 Government Bonds
  - 152 Corporation Bonds
  - 153 Corporation Stocks
  - 154 Building
    - 0154 Res. for Depr. of Building
  - 155 Land
- 16 Office Equipment
  - 016 Reserve for Depreciation of Office Equip.
- 17 Law Library
  - 017 Reserve for Depreciation of Law Library
- 18 Automobile
  - 018 Reserve for Depreciation of Automobile

II *Liabilities*
- 21 Accounts Payable
- 22 Employees' Income Taxes Pay.
- 23 Social Security Taxes Payable
- 24 Mortgages Payable

III *Proprietorship*
- 31 J. C. Allen, Proprietor
- 32 J. C. Allen, Drawing
- 33 Profit and Loss Summary

IV *Income*
- *41 Professional Income*
  - 411 Legal Fees
  - 412 Collection Fees
- *42 Investment Income*
  - 421 Interest Received
  - 422 Dividends Received
  - 423 Rent Received

V *Expenses*
- *51 Professional Expenses*
  - 511 Rent Expense
  - 512 Telephone and Telegraph Expense
  - 513 Salaries
  - 514 Social Security Taxes
  - 515 Stationery and Supplies
  - 516 Depreciation Expense
  - 517 Automobile Expenses
  - 518 Miscellaneous Expenses
- *52 Investment Expenses*
  - 521 Interest Paid
  - 522 Building Repairs
  - 523 Depr. of Building
- *53 Other Charges*
  - 531 Charitable Contributions

Law Library, Account No. 17. It is not uncommon for a lawyer to invest a considerable amount in a library of legal publications. Such a library constitutes an asset that should be treated in the same manner as other fixed assets that are subject to depreciation. The library account should be debited for the cost of the books purchased and should be credited for the cost of any books disposed of.

Reserve for Depreciation of Law Library, Account No. 017. Legal publications are subject to depreciation. Such depreciation is an allowable deduction in an income tax return; hence it is important that it be accounted for properly. The estimated amount of depreciation sustained each year should be recorded by debiting Depreciation Expense, Account No. 516, and by crediting Reserve for Depreciation of Law Library, Account No. 017. The reserve account is a valuation account. To ascertain the book value of a law library it is necessary to subtract the balance of the reserve account from the balance of the library account. It is customary to show this deduction in the balance sheet, extending the book value as the asset value of the library.

Accounts Payable, Account No. 21. A lawyer may incur a liability for accounts payable as a result of the following types of transactions:

(a) Purchases of equipment or other property on credit.

(b) Collections made for or on behalf of clients.

When equipment or other property is purchased on credit, the transaction should be recorded by debiting the proper asset account and by crediting Accounts Payable for the cost of the property. Even though the accounts are kept on the cash basis, property may be purchased on credit and such transactions should be recorded immediately in order that both the assets and the liabilities will be reflected in the accounts. This is particularly important where the property purchased is subject to depreciation, because depreciation is an expense that constitutes an allowable deduction for income tax purposes.

When collections are made for or on behalf of clients, the transactions should be recorded by debiting the bank checking account and by crediting (a) Collection Fees for the amount of the lawyer's commission and (b) Accounts Payable for the proceeds, represented by the difference between the amount collected and the amount of the lawyer's commission. When the proceeds are remitted to a client, the transaction should be recorded by debiting Accounts Payable and by crediting the bank checking account.

Mr. Allen does not keep a separate ledger account with each creditor. Purchase invoices representing the purchase of equipment or other property on credit are recorded in the combined cash-journal by debiting the proper asset account and by crediting Accounts Payable. The invoices are then filed in an unpaid invoice file where they are held until they are paid, at which time they are transferred to a paid invoice file. This is a method of handling invoices that is widely used by individuals engaged in personal service enterprises.

Legal Fees, Account No. 411. This account is an income account that is credited for cash received from clients in payment of legal fees. When the accounts are kept on the cash basis, no income is recorded in this account until it is received in cash or other property.

Collection Fees, Account No. 412. One source of income for many lawyers is fees charged clients for collecting accounts against their customers, patients, or clients. The collection fees account is an income account that should be credited for the commissions or fees received for collections made in behalf of clients. When a lawyer makes a collection in partial or in full settlement of an account, the transaction should be recorded by debiting the bank checking account for the amount received, by crediting Collection Fees for the amount of his commission, and by crediting Accounts Payable for the balance. Thus, if Lawyer A undertakes to collect an account amounting to $100 for Client B on a commission basis of 15 per cent, the following entry should be made when a remittance is received in payment of the account:

Debit the bank checking account	$100.00	
Credit Collection Fees		$15.00
Credit Accounts Payable		85.00

When Lawyer A remits the proceeds, amounting to $85, to Client B, an entry should be made as follows:

Debit Accounts Payable	$85.00	
Credit the bank checking account		$85.00

If desired, a separate checking account may be opened at the bank in which all cash, checks, and other cash items received in settlement of collection cases may be deposited. Some lawyers consider it advisable to segregate such deposits from the deposits in their regular checking account. When a separate bank account is maintained for this purpose, all checks drawn in favor of clients for the purpose of remitting the proceeds of collections should be credited to that account instead of to the regular checking account.

Investment Accounts. Reference to Mr. Allen's chart of accounts reveals that Accounts Nos. 151 to 155 inclusive are investment accounts. It will also be noted that Accounts Nos. 421 to 423 inclusive are investment income accounts, while Accounts Nos. 521 to 523 inclusive are investment expense accounts. Persons engaged in professional or other personal service enterprises may invest their surplus funds in either real or personal property. A record of such investments should be kept. In maintaining an adequate record of investments, it is advisable to keep separate property, income, and expense accounts in order that the investments may be accounted for entirely separate from the enterprise itself.

Real Property. Individuals engaged in personal service enterprises frequently make investments in real property. *Real property* includes land, whether laid out in town lots or otherwise, buildings, structures, improvements, and fixtures of whatever kind thereon, and all rights and privileges belonging or appertaining thereto. Real estate may consist of either city property or farm property.

In accounting for the cost of real property, it is advisable to keep separate accounts for the land and the buildings because the buildings only are subject to depreciation. When real property is acquired, the total cost should be allocated between the land and the buildings. For example, if apartment property is purchased as an investment at a cost of $75,000, the cost should be allocated between the lot and the building on a reasonable basis. The lot might be valued at $5,000 and the building at $70,000. It is necessary to take into consideration the depreciation sustained on buildings in computing the gain or loss resulting from a sale or an exchange of the property.

Land. When land is purchased as an investment, whether it be city lots, farm land, or undeveloped land, a land account should be debited for the cost. The usual plan is to open an account for such land with a title that is descriptive of the land in respect to its location. For example, the title of an account representing a city lot might be "Lot No. 10, Observatory Subdivision." After the account is debited for the original cost of the land, it should be debited for any additional expenditures constituting improvements, such as the cost of assessments for sidewalks, streets, sewers, highways, or other permanent improvements that tend to enhance the value of the land.

Example: Dr. A. C. Dolan purchased Lot No. 14 in Fairview Subdivision as an investment, paying $4,000 cash for it. Subsequently expenditures for improvements were made as follows:

Assessment for paving street..............................	$1,000.00
Assessment for sidewalk....................................	200.00
Assessment for sewer..	100.00

All of the costs incurred are shown recorded in the following "T" account:

Lot No. 14, Fairview Subdivision		
Cost	4,000.00	
Street assessment	1,000.00	
Sidewalk "	200.00	
Sewer "	100.00	

When such land is sold, the account should be credited for the total cost including the original cost and subsequent expenditures for improvements. Any gain resulting from the sale should be recorded in a separate account entitled Gain from Sale of Real Property. Any loss resulting from the sale should be recorded in a separate account entitled Loss from Sale of Real Property. The land account will then be in balance after the sale is recorded.

Buildings. Accounting for buildings is somewhat more complicated than accounting for land, although the general principles are the same. When real property is acquired through purchase, the value allocated to any buildings located on the land should be recorded in separate accounts. Thus, in the case of city property it may be necessary to keep separate accounts with the lot, the residence, and the garage (if the garage is separate from the residence). In the case of farm property it may be necessary to keep separate accounts with the land, the house, and the barn.

It can be understood readily why separate accounts with each type of property should be kept. If any loss is sustained that is deductible for income tax purposes, the amount of that loss must be ascertained. Unless the cost of real property is allocated separately to the land and the buildings at the time of purchase and separate accounts are maintained with each, it may be difficult subsequently to arrive at the information needed in (a) computing the gain or the loss derived from the sale or exchange of each type of property, or (b) determining, either for the purpose of an insurance settlement or for income tax purposes, the amount of a fire loss sustained.

Another reason for keeping separate accounts with different buildings is that the type of construction largely determines the rate of depreciation. Obviously, a frame building may depreciate more rapidly than one of brick, concrete, or metal construction.

When buildings are used for business purposes or are held for investment purposes, the depreciation sustained on such buildings is a business expense and is an allowable deduction for income tax purposes.

Example: Dr. Dolan had an apartment building constructed on Lot No. 14, Fairview Subdivision at a total cost of $54,000. The building was estimated to have a useful life of fifty years; hence each year Dr. Dolan charged off depreciation at the rate of 2 per cent per year, recording the depreciation by debiting an account entitled Depreciation of Apartment Building and by crediting an account entitled Reserve for Depreciation of Apartment Building for $1,080. After depreciation had been charged off for three years, the building and the reserve accounts appeared on his ledger as shown in the following "T" accounts:

APARTMENT BUILDING

Cost	54,000.00		

RESERVE FOR DEPRECIATION OF APARTMENT BUILDING

		Depr. first year	1,080.00
		Depr. second year	1,080.00
		Depr. third year	1,080.00

If, at the end of the third year after constructing the apartment building, Dr. Dolan sold the property for $62,500, the transaction should be recorded as indicated in the following general journal entry:

Cash	$62,500.00	
Reserve for Depr. of Apartment Building	3,240.00	
Lot No. 14, Fairview Subdivision		$ 5,300.00
Apartment Building		54,000.00
Gain from Sale of Real Property		6,440.00
Sold apartment property.		

Real Property Income. When real property is held as an investment and income is derived from rentals, a separate account should be kept for recording the rent received. If other income is received from such property, it should be recorded in separate accounts. For example, if income is derived from advertising privileges, such as billboards erected on the property, a separate account of such income should be kept.

Real Property Expenses. A separate account should be kept for each type of expense sustained in connection with the ownership of real property. In accounting for real property expenses, such as taxes, insurance, depreciation, repairs, and interest on money borrowed to purchase the property, it is necessary to consider the purpose for which the property was purchased or is used. Certain expenses, such as insurance premiums, repairs, and depreciation, are deductible in computing net income for the purpose of the income tax when they apply to property purchased for investment purposes or property owned for business purposes. On the other hand such expenses are not deductible when they apply to property used by a taxpayer for residential purposes. The purpose for which property is acquired determines whether or not certain expenses represent business expenses or personal expenses.

The following schedule of expenses sustained in connection with the ownership of real property shows which expenses are deductible and which are not deductible in arriving at net income for income tax purposes:

SCHEDULE OF REAL PROPERTY EXPENSES AND LOSSES

Items	Property Owned As Investment		Property Used As Residence	
	Deductible	Non-Deductible	Deductible	Non-Deductible
Property taxes on land......	x		x	
Property taxes on buildings..	x		x	
Interest on money borrowed to purchase land.........	x		x	
Interest on money borrowed to construct buildings.....	x		x	
Insurance on buildings......	x			x
Depreciation on buildings....	x			x
Repairs to buildings.........	x			x
Wages of caretaker of buildings.....................	x			x
Heating and lighting costs....	x			x
Casualty losses resulting from fire, storm, flood, etc., not covered by insurance......	x		x	
Losses from sale of real property...................	x			x
Street improvement assessment....................		x		x

Separate accounts should be kept for deductible and nondeductible expenses that may be sustained in connection with the ownership of real property. When the accounts are kept on the cash basis, such expenses as taxes, interest, insurance, and repairs should be recorded when actually paid, regardless of when they are incurred.

In the case of depreciation of buildings, the amount of the depreciation should be estimated and the estimated amount should be recorded before the books are closed at the end of the year. In estimating the amount of the depreciation, it is necessary to take into consideration the following factors:

(a) Cost of the buildings.
(b) Probable life of the buildings.

There are different methods of computing depreciation. A simple method is to divide the cost by the probable life of the building to find the estimated amount of the annual depreciation. Thus, if a building costs $20,000 and has an estimated life of fifty years, the annual depreciation will amount to 2 per cent of the cost, or $400 a year. A simple method of recording the depreciation is indicated by the following general journal entry:

Building Expenses	$400.00	
Reserve for Depreciation of Building		$400.00
Depreciation of building at 2% for one year.		

Taxable Income. Since any income derived from the ownership of real property is taxable under the income tax laws, it is obvious that a record of such income should be kept. If an individual purchases apartment property as an investment and keeps separate accounts for the land, the building, the rent income, and each type of expense, at the end of each year he may compute his net income from rents in the following manner:

Gross income from rents		$3,600.00
Deduct operating expenses:		
Depreciation	$600.00	
Repairs	100.00	
Taxes	500.00	
Insurance	60.00	
Interest on mortgage	500.00	
Wages of caretaker	480.00	
Gas and electricity	400.00	2,640.00
Net income from apartment property		$ 960.00

Such a schedule will provide the information needed by the owner of apartment property in preparing his income tax returns.

Gains and Losses from Sales of Real Property. Any gain derived from the sale of real property, whether it is held for investment purposes or for personal residential use, is taxable and should be recorded in a separate account. Any loss sustained from the sale of real property should also be recorded in a separate account. The loss may or may not be deductible in computing net income for income tax purposes. When property is purchased for investment purposes and is subsequently sold at a loss, the loss is deductible. When property is purchased and used by the taxpayer for residential purposes, any loss resulting from the subsequent sale of the property is considered a personal loss and is, therefore, not an allowable deduction in computing net income for income tax purposes.

Real Estate Records. When investments in real property involve the ownership of a number of different properties, it may be advisable for the owner to keep a supplementary or auxiliary record of each property. Special forms similar to the one shown in Illustration No. 23 may be used for this purpose. The forms are so designed that all necessary information may be recorded conveniently thereon. The form is designed to facilitate recording a complete description of the property owned, together with the investment record and a record of whatever insurance is carried on the property. The information recorded on such a form is supplementary to the information recorded in the regular books of account.

RECORD OF REAL ESTATE

NAME OF PROPERTY Fairview Apartments
LOT 120 FEET FRONT ON Highland STREET BY 201 FEET DEEP BETWEEN Cornell STREET AND Madison
IMPROVEMENTS Two-family Apartment

VALUE OF LAND $ 5,150.00
VALUE OF IMPROVEMENTS 24,000.00
TOTAL VALUE $ 29,150.00

LEGAL DESCRIPTION

MORTGAGE $ 10,000 DUE December 31, 1960 INTEREST FROM December 31, 1950 AT 5 %
MORTGAGEE Union Trust Co. INTEREST PAYABLE Semiannually WHERE Bank

INVESTMENT RECORD						INSURANCE			
DATE 1950		DESCRIPTION	PURCHASE PRICE	DEVELOPMENT & IMPROVEMENTS	SOLD FOR	COMPANY OR AGENT	POLICY NUMBER	EXPIRATION	AMOUNT
Jan.	2	Lot No. 14	4000 00						
June	30	Assessment-street		1000 00					
	30	" -sidewalk		100 00					
	30	" -sewer		50 00					
Dec.	31	Apt. Building		24000 00					
Dec.	31				32500 00				

Illustration No. 23, Record of Real Estate

Books of Account. Mr. Allen uses the following books of account:

(a) General books
 Combined cash-journal
 General ledger

(b) Auxiliary records
 Petty cash disbursements record
 Lawyers' case docket
 Lawyers' collection docket

Combined Cash-Journal. The form of combined cash-journal that is best suited to the needs of an individual engaged in a personal service enterprise differs somewhat from the form of combined cash-journal that is suited to the needs of a mercantile enterprise. Reference to Mr. Allen's combined cash-journal reproduced on page 251 reveals that he uses eight-column standard ruled paper like that used in W. L. Mann's combined cash-journal reproduced on page 176. However, there is a difference in the headings of the columns. The columnar arrangement of Mr. Allen's combined cash-journal is as follows:

(a) First National Bank
  (1) Deposits, Dr.
  (2) Checks, Cr.
(b) General
  (3) Debits
  (4) Credits
(c) Income
  (5) Legal Fees, Cr.
  (6) Collection Fees, Cr.
(d) Wage Deductions
  (7) Employees' Income Taxes Payable, Cr.
  (8) S. S. Taxes Payable, Cr.

The account numbers are also indicated in the headings. This is an aid in completing the summary posting at the end of each month.

Mr. Allen's principal sources of income are (a) legal fees and (b) collection fees. Since separate accounts are kept for each of these sources of income, it is desirable to provide a separate amount column in the combined cash-journal for recording the income from each source. Any income derived from other sources is recorded in the General Cr. column.

The last two amount columns are used for recording the amounts withheld from the wages paid to Mr. Allen's employees for federal income taxes and for federal old-age insurance benefits. Under the laws of some states it would also be necessary to withhold a percentage of the employees' wages for disability benefits or unemployment compensation purposes. Since Mr. Allen is not a resident of one of these states, no such withholding is required in his case.

Following is a narrative of transactions completed by Mr. Allen during the month of October. These transactions are recorded in the combined cash-journal reproduced on page 251.

NARRATIVE OF TRANSACTIONS

J. C. ALLEN, ATTORNEY AT LAW

Monday, October 2

Issued Check No. 201 for $90, payable to J. H. Walker, for the October office rent.

Tuesday, October 3

Issued Check No. 202 for $4.09 to the Public Service Electric Co. for electricity consumed during September.

The amount of this check was charged to Miscellaneous Expenses, Account No. 518, for the reason that a special expense account for electric service is not maintained.

Received $10 from Mrs. Laura Womack for services rendered in preparing an abstract of title.

Because the cash received from Mrs. Womack will be deposited in the checking account, the transaction was recorded by debiting First National Bank — Checking, Account No. 111, and by crediting Legal Fees, Account No. 411. Since individual posting of this entry is not required, a check mark was placed in the Posting Reference column.

Wednesday, October 4

Mr. Allen reports that he has been engaged by Dependable Motors, Inc., 1401 Reading Road, City, to represent them in a lawsuit against George Maher, 3450 May St., City, at a minimum fee of $110 and costs, and that he has received their check for $50 as a retainer. Case No. 103.

The amount received as a retainer constitutes income realized on the cash basis. Case Docket No. 103 is reproduced on page 253. This docket is an auxiliary record of information designed to supplement the information recorded in the regular books of account and to facilitate the handling of the case.

Issued Check No. 203 for $12.50 to Miss Clara Hazelton, a public stenographer, for stenographic services.

Issued Check No. 204 for $4.95 to the Bell Telephone Co. for the September service invoice.

Thursday, October 5

Received a check for $100 from W. R. Halsey in payment of the balance due on Case No. 94.

Received a check for $90 from the Automotive Accessories Co. in full payment of Case No. 96.

Friday, October 6

Issued Check No. 205 for $19.12 to Harry's Friendly Service Station in payment of the October 1 statement, covering gasoline, oil, and services rendered during September.

Received for collection from The H. & S. Pogue Co., Fourth and Race Streets, City, a statement of its account with S. L. Hale, 1642 Paxton Road, City, for $130. This account is over eighteen months past due. Collection fee, 25%; no suit without further instructions. Collection No. 51.

Inasmuch as Mr. Allen's books are kept on the cash basis, no entry in the regular books of account is required for this transaction. Collection Docket No. 51 is reproduced on page 255. This docket is an auxiliary record of information designed to supplement the information recorded in the regular books of account and to facilitate handling the account.

Saturday, October 7

Proved the footings of the combined cash-journal. Deposited $250 in the checking account at the First National Bank and proved the bank balance ($2,699.37).

The individual posting was completed at this time. As each item was posted from the General columns of the combined cash-journal to the proper ledger account, the account number was entered in the Posting Reference column.

Monday, October 9

Received $20 from The Keith Co. for services rendered in connection with preparing a mortgage.

The waved lines appearing at this point in the combined cash-journal indicate omission of the transactions completed on the days between October 9 and 31.

Tuesday, October 31

Issued Check No. 215 for $35.60 to Robert Hamilton, part-time law clerk in payment of one-half month's salary amounting to $40, less 60 cents withheld for federal old-age insurance benefits, and $3.80 withheld for federal income taxes.

Issued Check No. 216 for $43.45 to the office secretary, in payment of one-half month's salary amounting to $50, less 75 cents withheld for federal old-age insurance benefits, and $5.80 withheld for federal income taxes.

Issued Check No. 217 for $16.20 to the Collector of Internal Revenue in payment of the social security taxes on the wages paid to employees during the quarter ended September 30.

Since Mr. Allen keeps his accounts on the cash basis, he does not record the tax imposed on employers for old-age and survivors' insurance benefits until the tax is paid. In recording this transaction, it was, therefore, necessary to debit Social Security Taxes, Account No. 514, for the employer's share of the tax and to debit Social Security Taxes Payable, Account No. 23, for the employees' share of the tax.

(Continued on page 252)

COMBINED CASH-JOURNAL FOR MONTH OF October 19–

FIRST NATIONAL BANK		DATE		DESCRIPTION	POST. REF.	GENERAL		INCOME		WAGE DEDUCTIONS	
DEPOSITS 111 DR.	CHECKS 111 CR.	MO.	DAY			DEBITS	CREDITS	LEGAL FEES 411 CR.	COLLECTION FEES 412 CR.	EMPLOYEES' I. T. PAY. 22 CR.	S. S. TAXES PAY. 23 CR.
				AMOUNTS FORWARDED							
		Oct.	1	Balance $2,580.03	✓						
	90 00		2	Rent Expense #201	511	90 00					
	4 09		3	Misc. Expenses #202	518	4 09					
10 00			3	Mrs. Laura Womack, Abstract	✓			10 00			
50 00			4	Dependable Motors, Inc., Case #103	✓			50 00			
	12 50		4	Misc. Expenses #203	518	12 50					
	4 95		4	Tel. & Tel. Expense #204	512	4 95					
100 00			5	W. R. Halsey, Case #94	✓			100 00			
90 00			5	Automotive Accessories Co., Case #96	✓			90 00			
	19 12		6	Automobile Expense #205 $2,697.37	517	19 12					
20 00			9	The Keith Co., Mortgage	✓			20 00			
	35 60		31	Salaries #215	513	40 00				3 80	60
	43 45		31	Salaries #216	513	50 00				5 80	75
	16 20		31	Social Security Taxes #217	514	8 10					
				Social Security Taxes Pay.	23	8 10					
	57 60		31	Employees' Income Taxes Pay. #218	22	57 60					
	29 05		31	Advances in Behalf of Clients #219	14	8 00					
				J. C. Allen, Drawing	32	5 00					
				Tel. & Tel. Expense	512	1 35					
				Stationery & Supplies	515	2 95					
				Automobile Expenses	517	2 00					
				Misc. Expenses	518	7 75					
				Charitable Contributions	531	2 00					
1365 45	1338 16					1359 55	495 34	705 00	165 11	19 20	2 25
(111)	(111)					(✓)	(✓)	(411)	(412)	(22)	(23)

Combined Cash-Journal for a Personal Service Enterprise

Issued Check No. 218 for $57.60 to the Collector of Internal Revenue in payment of the income taxes withheld from the wages paid to employees during the quarter ended September 30.

Issued Check No. 219 for $29.05 to replenish the petty cash fund.

The following statement provided the information needed in recording this transaction in the combined cash-journal:

STATEMENT OF PETTY CASH DISBURSEMENTS FOR OCTOBER

Advances in Behalf of Clients	$ 8.00
J. C. Allen, Drawing	5.00
Telephone and Telegraph Expense	1.35
Stationery and Supplies	2.95
Automobile Expenses	2.00
Miscellaneous Expenses	7.75
Charitable Contributions	2.00
Total Disbursements	$29.05

Proved the footings, entered the totals, and ruled the combined cash-journal. Proved the bank balance ($2,607.38).

The individual posting from the General columns of the combined cash-journal was completed at this time. Since this is the end of the month, the summary posting of the totals of the special columns was also completed. As the summary posting was completed, the account numbers were written immediately below the totals of the columns in the combined cash-journal.

General Ledger. The general ledger used by a personal service enterprise may be either a bound book or a loose-leaf book. Either the standard account form (Illustration No. 2) or the balance account form (Illustration No. 17) may be used. The standard account form is generally preferred for general ledger accounts. The accounts should be arranged in the general ledger in the order in which they appear in the chart of accounts. If the accounts are numbered they should, of course, be arranged in numerical order. Inasmuch as the combined cash-journal is the only book of original entry used by Mr. Allen, all posting to the general ledger accounts is from this journal. Proof of equality of the general ledger account balances is ascertained at the end of each month by taking a trial balance. Mr. Allen's trial balance as of October 31 is reproduced in the first two amount columns of his work sheet illustrated on page 258.

Auxiliary Records. Auxiliary records are used to record information which is supplemental to that recorded in the regular books of account. In addition to the regular books of account, Mr. Allen uses a petty cash disbursements record, a case docket, and a collection docket, as auxiliary records.

LAWYERS' CASE DOCKET

IN THE Common Pleas COURT — COURT FILE NO. A 10905

COUNTY Hamilton, State of Ohio — OFFICE FILE NO. 103

PARTIES	NATURE OF CASE
Dependable Motors, Inc	ACTION Lawsuit
1401 Reading Road	
City	AMOUNT Minimum fee, $110.00
	with costs
PLAINTIFF	
VS.	
George Maher	ATTORNEYS FOR PLAINTIFF
	ATTORNEYS FOR DEFENDANT
DEFENDANT	

DATE		PROCEEDINGS IN CAUSE AND DISPOSITION OF CASE
19— Oct	9	Suit filed
		DATE OF JUDGMENT — AMOUNT $

DATE		DESCRIPTION	✓	CHARGES	DATE		DESCRIPTION	✓	CREDITS
19— Oct	4	Case Received	✓	110 00	19— Oct	4	Retainer	CJ	50 00
	9	Suit Fee	PC	3 00	Nov	2	In full	CJ	63 00

Illustration No. 21, Lawyers' Case Docket

Petty Cash Disbursements Record. Mr. Allen maintains a petty cash fund amounting to $50. The form of the petty cash disbursements record used by Mr. Allen is the same as that illustrated on page 179. Accounts Nos. 14, 32, 512, 515, 517, 518, and 531 are inserted in the headings of the Distribution columns to facilitate classification of the expenditures.

Lawyers' Case Docket. Lawyers usually use a form known as a *case docket* to maintain a memorandum record of each legal case with a client from the time it is accepted until it is finally disposed of. A model filled-in copy of a case docket is reproduced in Illustration No. 24. This docket provides a history of the case of Dependable Motors, Inc., plaintiff, vs. George Maher, defendant. It also provides a record of the charges and credits to the account of the client — Dependable Motors, Inc. The upper part of the form is designed to facilitate recording the legal information that may be needed in handling the case. The lower part of the form is designed to facilitate keeping a memorandum account with the client.

When a lawyer keeps his accounts on the cash basis he does not keep a summary account with clients in the general ledger as accounts receivable. However, it is necessary to keep a memorandum account with each client. The account form on the case docket serves this purpose. The client's account should be charged for —

(a) Fees for services rendered.

(b) Advances in behalf of the client, such as court costs and other expenses paid in his behalf.

The fees to be charged for services may be agreed upon in advance, in which case they may be recorded when opening the memorandum account on the case docket. Otherwise, the fees are not recorded until the case is settled and the amount determined.

The client's account should be credited for —

(a) Payments received for services.

(b) Payments received as reimbursement for advances made in behalf of the client.

In Illustration No. 24 the client, Dependable Motors, Inc., is charged for the following:

October 4. Amount of the fee agreed upon at the time the case was taken, $110.

October 9. Amount advanced in payment of suit fee, $3.

The account is credited for the following:

October 4. Amount received as a retainer, $50.

November 2. Amount received in payment of balance due on account, $63.

LAWYERS' COLLECTION DOCKET No. 51

DEBTOR S. L. Hale	DATE CLAIM REC'D Oct. 6 19–
ADDRESS 1642 Paxton Road, City	DATE DISPOSED OF Nov. 14, 19–
BUSINESS	TOTAL AMOUNT $130.00
CREDITOR The H. & S. Pogue Co.	AMOUNT COLLECTED $130.00
ADDRESS Fourth and Race Streets, City	FEES $32.50
REC'D CLAIM FROM	EXPENSE $
ATTORNEY FOR DEBTOR	AMOUNT REMITTED $97.50
CALLS ON DEBTOR	CHECK NO. 231

	RECEIVED FROM CREDITOR		
	DATE	FOR	AMOUNT
CORRESPONDENCE	Nov. 6–	Com.	10.00
	Nov. 9–	Com.	22.50

RECEIVED FROM DEBTOR				PAID TO CREDITOR			
DATE	AMOUNT	DATE	AMOUNT	CHECK NO.	AMOUNT	CHECK NO.	AMOUNT
Nov. 6–	40.00			231	97.50		
9–	90.00						

REMARKS: Statement of account. Collection fee, 25%. No suit without further instructions.

Illustration No. 25, Lawyers' Collection Docket

Lawyers' Collection Docket. Lawyers who handle collections for clients usually use a form known as a *collection docket* to maintain a record of the essential data pertaining to collections. A model filled-in copy of a collection docket is reproduced in Illustration No. 25. This docket provides a history of the case of The H. & S. Pogue Co., creditor, vs. S. L. Hale, debtor. It also provides a record of the amounts collected from the debtor and the amounts paid to the creditor.

Lawyers take most collection cases on a percentage basis. The charges for collection services are thus based on the collections actually made. Since a lawyer's only compensation for making collections usually is a percentage of the amount collected, any expenses incurred in making collections should be charged to the usual expense accounts of the lawyer and not to the client. However, if a client has agreed to stand any expenses, such as for example, court costs incident to a law suit, amounts paid by the lawyer should be charged to the client's account just the same as amounts advanced in behalf of clients in handling other legal cases.

In Illustration No. 25 the following transactions are shown recorded on the collection docket for The H. & S. Pogue Co.:

November 6. Collected $40 from S. L. Hale, debtor.
November 9. Collected $90 from S. L. Hale, debtor.
November 13. Paid $97.50 to The H. & S. Pogue Co., creditor.

The amounts received from the creditor in payment of the lawyer's commission is also recorded on the collection docket. Since his commission of 25 per cent was actually deducted from the amounts collected from the debtor, it will be noted that the amounts deducted are entered as follows:

November 6. $10.
November 9. $22.50.

Work at the Close of the Fiscal Period. The work required at the close of the fiscal period in keeping the accounts for a personal service enterprise is similar to that required for any other enterprise. The accounts should be analyzed and any required adjustments made. A balance sheet and a profit and loss statement should be prepared. The temporary accounts should be closed. A work sheet is an aid in compiling and classifying the information needed in preparing the financial statements and in drafting the adjusting and closing entries.

A Work Sheet for a Personal Service Enterprise. The work sheet reproduced on page 258 is based on the accounts of J. C. Allen, an attorney at law. His accounts are kept on the cash basis and the work sheet reflects the results of operations for the ten-months' period ended October 31. It will be noted that the form of this work sheet is the same as the work sheet for a mercantile enterprise reproduced on pages 196 and 197. Mr. Allen's trial balance as of October 31 was copied in the first two amount columns.

The required adjustments of certain account balances were entered in the third and fourth amount columns. When the accounts are kept on the cash basis, few adjustments are required; usually, however, it is necessary to make adjustment for the amount of depreciation sustained during the period. Other adjustments may also be necessary. For example, if U. S. Savings Bonds are owned and it is desired to report the interest on the accrual basis in the income tax return (which is permissible even when the accounts are kept on the cash basis), any interest accrued on such bonds at the close of the accounting period should be recorded on the work sheet.

In preparing the work sheet for Mr. Allen, the only adjustments required were those needed to record the amount of depreciation sustained during the accounting period. He estimated that he had sustained depreciation as follows:

(a) Office equipment, 10 per cent a year.
(b) Law library, 5 per cent a year.
(c) Automobile, 25 per cent a year.

These rates indicate that Mr. Allen estimated that his office equipment had a useful life of ten years, his law library twenty years, and his automobile four years. He had also ascertained that he would be permitted to claim such depreciation as an allowable deduction in his income tax return for each year during the life of the property.

The basis for computing the depreciation is the original cost of the assets. Since this work sheet was prepared as of October 31, the depreciation was computed for a period of ten months only. The calculations were as follows:

Office Equipment, 10% of $600 for 10 months..............	$ 50.00
Law Library, 5% of $2,000 for 10 months..................	83.33
Automobile, 25% of $1,200 for 10 months..................	250.00
Total Depreciation for 10 months.......................	$383.33

The depreciation was recorded on the work sheet by debiting Depreciation Expense for $383.33, and by crediting Reserve for Depreciation of Office Equipment for $50, Reserve for Depreciation of Law Library for $83.33, and Reserve for Depreciation of Automobile for $250,

J. C. Allen

Work Sheet for Ten-Months' Period Ended October 31, 19–

Accounts	Acct. Nos.	Trial Balance Dr. Balances	Trial Balance Cr. Balances	Adjustments Debits	Adjustments Credits	Adj. Trial Balance Dr. Balances	Adj. Trial Balance Cr. Balances	Profit and Loss Dr. Balances	Profit and Loss Cr. Balances	Balance Sheet Dr. Balances	Balance Sheet Cr. Balances
First National Bank-Checking	111	2607 38				2607 38				2607 38	
First National Bank-Savings	112	600 00				600 00				600 00	
Petty Cash Fund	12	50 00				50 00				50 00	
Adv. in Behalf of Clients	14	8 00				8 00				8 00	
Government Bonds	151	8000 00				8000 00				8000 00	
Office Equipment	16	600 00				600 00				600 00	
Res. for Depr. of Office Equip.	016		175 00		50 00		225 00				225 00
Law Library	17	2000 00				2000 00				2000 00	
Res. for Depr. of Law Library	017		400 00		83 33		483 33				483 33
Automobile	18	1200 00				1200 00				1200 00	
Res. for Depr. of Automobile	018		250 00		250 00		500 00				500 00
Accounts Payable	21		50 00				50 00				50 00
Employees' Income Taxes Pay.	22		19 20				19 20				19 20
Social Security Taxes Pay.	23		2 70				2 70				2 70
J. C. Allen, Proprietor	31		10924 63				10924 63				10924 63
J. C. Allen, Drawing	32	3981 50				3981 50				3981 50	
Legal Fees	411		9943 12				9943 12		9943 12		
Collection Fees	412		481 23				481 23		481 23		
Interest Received	421		130 96				130 96		130 96		
Rent Expense	511	900 00				900 00		900 00			
Tel. & Tel. Expense	512	44 75				44 75		44 75			
Salaries	513	1755 00				1755 00		1755 00			
Social Security Taxes	514	32 40				32 40		32 40			
Stationery & Supplies	515	192 65				192 65		192 65			
Depreciation Expense	516			383 33		383 33		383 33			
Automobile Expenses	517	291 28				291 28		291 28			
Miscellaneous Expenses	518	81 88				81 88		81 88			
Charitable Contributions	531	32 00				32 00		32 00			
		22376 84	22376 84	383 33	383 33	22760 17	22760 17	3713 29	10555 31	19046 88	12204 86
Net Income								6842 02			6842 02
								10555 31	10555 31	19046 88	19046 88

Work Sheet for a Personal Service Enterprise

After entering the required adjustments on the work sheet and proving the footings, the adjusted account balances were extended to the Adjusted Trial Balance columns. After proving the footings of the Adjusted Trial Balance columns, the account balances were classified by extending the balance of each account to the proper column. The net income for the period was then ascertained by footing the Profit and Loss columns and by ascertaining the difference between the footings. This difference amounted to $6,842.02. The Balance Sheet columns were then footed and the difference ascertained. This difference amounting to $6,842.02 represents the net increase in proprietorship for the period. When the balance sheet is correctly prepared, the difference between the footings of the Balance Sheet columns will always be the same as the difference between the footings of the Profit and Loss columns.

Balance Sheet of a Personal Service Enterprise. The function of a balance sheet of a personal service enterprise is the same as that of any other enterprise. It may be prepared either in account form or in report form and it may be penwritten or typewritten. Mr. Allen's balance sheet, prepared in account form, is reproduced on page 260. His work sheet, reproduced on page 258, provided the information needed in preparing his balance sheet. A comparison of Mr. Allen's balance sheet with the balance sheet of W. L. Mann reproduced on page 206 shows that they are similar in form and that the accounts are classified in a similar manner.

The amount of cash listed as an asset in Mr. Allen's balance sheet is the sum of the following:

Bank checking account	$2,607.38
Bank savings account	600.00
Petty cash fund	50.00
Total	$3,257.38

In an enterprise where the income is derived primarily from personal services rendered, the ratio of current assets to current liabilities may have little significance as compared with a mercantile enterprise. This is particularly true of professional enterprises. If the accounts are kept on the cash basis, amounts due from clients, patients, or customers will not be included among the current assets. Furthermore, the accounts payable of a professional enterprise may bear little or no relationship to the income since no accounts payable are incurred in connection with the purchase of merchandise for sale.

J. C. ALLEN, ATTORNEY AT LAW

BALANCE SHEET, OCTOBER 31, 19—

ASSETS

Current Assets:			
Cash		$3,257.38	
Advances in Behalf of Clients		8.00	
Government Bonds		8,000.00	
Total Current Assets			$11,265.38
Fixed Assets:			
Office Equipment	$ 600.00		
Less Reserve for Depr.	225.00	$ 375.00	
Law Library	$2,000.00		
Less Reserve for Depr.	483.33	1,516.67	
Automobile	$1,200.00		
Less Reserve for Depr.	500.00	700.00	
Total Fixed Assets			2,591.67
Total Assets			$13,857.05

LIABILITIES

Current Liabilities:			
Accounts Payable		$ 50.00	
Employees' Income Taxes Payable		19.20	
Social Security Taxes Payable		2.70	
Total Current Liabilities			$ 71.90

PROPRIETORSHIP

J. C. Allen, Proprietorship,			
January 1, 19—		$10,924.63	
Net Income	$6,842.02		
Less Withdrawals	3,981.50	2,860.52	
Proprietorship, October 31, 19—			13,785.15
Total Liabilities and Proprietorship			$13,857.05

Balance Sheet of a Personal Service Enterprise

Profit and Loss Statement of a Personal Service Enterprise. The function of the profit and loss statement of a personal service enterprise is the same as that of any other enterprise. It is usually prepared in report form. Since a profit and loss statement provides information as to the results of operations over a period of time, it is particularly important that the length of the period covered be indicated in the heading of the statement. In Mr. Allen's profit and loss statement, reproduced on page 262, the heading indicates that the statement is "for the ten-months' period ended October 31."

In a professional enterprise the income accounts should be classified as follows:

(a) Professional income.
(b) Investment income and gains.
(c) Other income.

Professional income includes all income derived from professional services, such as legal fees and collection fees received by a lawyer, medical fees received by a physician, dental fees received by a dentist, and the fees received by public accountants, architects, engineers, and other professional persons.

Investment income and gains include all income derived from investments, such as interest received on bonds owned, dividends received on corporation stock owned, rents received on property owned, and gains derived from the sale of investment property.

Other income includes income or profits derived from any other source, such as gains derived from the sale of fixed assets.

Mr. Allen's work sheet, reproduced on page 258, provided the information needed in preparing his profit and loss statement. The statement shows that his professional income consisted of legal fees and collection fees. He also had some investment income derived from interest received.

The expenses of a professional enterprise should be classified as follows:

(a) Professional expenses.
(b) Investment expenses and losses.
(c) Other charges.

Professional expenses include all expenses incurred in the conduct of a profession, such as rent expense, automobile expenses, depreciation expense, salaries, social security taxes, and all similar expenses.

J. C. ALLEN, ATTORNEY AT LAW

PROFIT AND LOSS STATEMENT

For Ten-Months' Period Ended October 31, 19--

Professional Income:		
Legal Fees	$9,943.12	
Collection Fees	481.23	
Total Professional Income		$10,424.35
Professional Expenses:		
Rent Expense	$ 900.00	
Telephone and Telegraph Expense	44.75	
Salaries	1,755.00	
Social Security Taxes	32.40	
Stationery and Supplies	192.65	
Depreciation Expense	383.33	
Automobile Expenses	291.28	
Miscellaneous Expenses	81.88	
Total Professional Expenses		3,681.29
Net Professional Income		$ 6,743.06
Investment Income:		
Interest Received		130.96
		$ 6,874.02
Other Charges:		
Charitable Contributions		32.00
Net Income		$ 6,842.02

Profit and Loss Statement of a Personal Service Enterprise

Investment expenses and losses include all expenses and losses incurred in connection with investments, such as interest paid on a mortgage, building repairs, depreciation of buildings, caretaker's wages, property taxes, and losses sustained from the sale of investment property.

Other charges include any items paid or losses sustained that have no direct relation to the conduct of the profession or to investments, such as charitable contributions.

In the case of a professional enterprise, the fact should not be overlooked that the income is based primarily on services rendered rather than on capital invested. While some capital may be invested in a professional enterprise, it is not usually considered a direct income-producing factor. For that reason the ratio of the net income to the capital investment is likely to be much higher in a professional enterprise than in a mercantile enterprise where relatively large sums may be invested in merchandise and equipment.

Mr. Allen's profit and loss statement shows that his professional income, amounting to $10,424.35, was his principal income. Considering this sum as the base, or 100 per cent, it is possible to compute the various items on a percentage basis. For example, his professional expenses amounted to 35 per cent of his professional income, while his net income, amounting to $6,842.02, was equal to approximately 65 per cent of his total professional income.

Adjusting Entries for a Personal Service Enterprise. In order to bring the ledger accounts into agreement with the financial statements, any adjusting entries made on the work sheet must be posted to the proper accounts. Reference to Mr. Allen's work sheet reproduced on page 258 reveals that adjustments were made for the amount of depreciation sustained on the office equipment, law library, and automobile. Assuming that Mr. Allen's accounts are to be adjusted at the close of the period ended October 31, the required entries may be made in the combined cash-journal as shown in the illustration on page 264 in which a portion of his combined cash-journal is reproduced. The adjusting entries should be posted individually to the proper general ledger accounts. After the posting is completed the balances of the depreciation reserve accounts should be the same as the balances shown in the Balance Sheet columns of the work sheet, and in the balance sheet. The balance of the account with depreciation expense should be the same as the balance shown in the Profit and Loss columns of the work sheet and in the profit and loss statement.

Closing Entries for a Personal Service Enterprise. The information needed in drafting the closing entries for Mr. Allen was obtained from the Profit and Loss columns of his work sheet. The expense accounts are listed in the left-hand or debit column while the income accounts are listed in the right-hand or credit column under the heading of Profit and Loss. Since the income accounts have credit balances, it will be necessary to debit the accounts to close them. Since the expense accounts have debit balances it will be necessary to credit the accounts to close them. The closing entries should be made in the combined cash-journal as illustrated on page 264.

COMBINED CASH-JOURNAL

DATE MO.	DATE DAY	DESCRIPTION	POST REF	GENERAL DEBITS	GENERAL CREDITS
		AMOUNTS FORWARDED			
Oct.	31	Adjusting Entries:			
		Depr. Expense-Res. for Depr. O.E.		50 00	50 00
		" " -Res. for Depr. L.L.		83 33	83 33
		" " -Res. for Depr. Auto.		250 00	250 00
				383 33	383 33
	31	Closing Entries:			
		Legal Fees-P&L Summary		9943 12	9943 12
		Collection Fees- "		481 23	481 23
		Interest Received- "		130 96	130 96
		P&L Summary-Rent Expense		900 00	900 00
		" -T&T Expense		44 75	44 75
		" -Salaries		1755 00	1755 00
		" -S.S. Taxes		32 40	32 40
		" -Sta. & Sup.		192 65	192 65
		" -Depr. Expense		383 33	383 33
		" -Auto. Expenses		291 28	291 28
		" -Misc. Expenses		81 88	81 88
		" -Char. Contributions		32 00	32 00
		" -J. C. Allen, Draw.		3981 50	3981 50
		" -J. C. Allen, Prop.		2860 52	2860 52
				21110 62	21110 62

Adjusting and Closing Entries for a Personal Service Enterprise

In addition to closing the income and expense accounts, the profit and loss summary account should also be closed. The entries required to close this account depend upon what disposition the proprietor may wish to make of his net income for the period. During the period Mr. Allen withdrew $3,981.50 for personal use. It is logical to assume that he withdrew this sum from his income. Some accountants may prefer to consider withdrawals as a deduction from capital. A proprietor is likely to withdraw capital, however, only when he has more capital invested in an enterprise than is considered necessary, or when his income is insufficient to enable him to withdraw the amount needed for personal use and he is forced by necessity to withdraw a part of his capital. Since the amount withdrawn for personal use usually depends upon the amount of the income earned, it is more logical to assume that the proprietor's withdrawals represent a partial distribution of his current net income.

Mr. Allen's balance sheet, reproduced on page 260 shows that his withdrawals were treated as a deduction from his net income for the period. The remainder of the net income was added to the amount of his proprietorship at the beginning of the period and the sum extended as his proprietorship at the close of the period. This indicates that Mr. Allen did not desire to withdraw the balance of his current net income immediately. In closing the profit and loss summary account, therefore, a sufficient amount of the net income should be transferred to the proprietor's drawing account to balance that account. The remainder of the net income should be transferred to the proprietor's capital account.

The closing entries should be posted individually to the proper general ledger accounts. After posting the closing entries, all of Mr. Allen's temporary proprietorship accounts should be in balance. In posting to the profit and loss summary account, it is advisable to identify the accounts in the following manner:

PROFIT AND LOSS SUMMARY — Account No. 33

19--			19--		
Oct. 31	Rent Expense	900.00	Oct. 31	Legal Fees	9,943.12
31	Tel. & Tel. Expense	44.75	31	Collection Fees	481.23
31	Salaries	1,755.00	31	Interest Received	130.96
31	Social Security Taxes	32.40			*10,555.31*
31	Stationery & Supplies	192.65			
31	Depreciation Expense	383.33			
31	Automobile Expenses	291.28			
31	Misc. Expenses	81.88			
31	Char. Contributions	32.00			
31	J. C. Allen, Drawing	3,981.50			
31	J. C. Allen, Prop.	2,860.52			
		10,555.31			
		10,555.31			10,555.31

Post-Closing Trial Balance. After posting the closing entries, it is advisable to take a post-closing trial balance as a means of proof. Mr. Allen's post-closing trial balance is reproduced on the following page.

J. C. ALLEN

POST-CLOSING TRIAL BALANCE, OCTOBER 31, 19--

First National Bank — Checking	$ 2,607.38	
First National Bank — Savings	600.00	
Petty Cash Fund	50.00	
Advances in Behalf of Clients	8.00	
Government Bonds	8,000.00	
Office Equipment	600.00	
Res. for Depr. of Office Equipment		$ 225.00
Law Library	2,000.00	
Res. for Depr. of Law Library		483.33
Automobile	1,200.00	
Res. for Depr. of Automobile		500.00
Accounts Payable		50.00
Employees' Income Taxes Payable		19.20
Social Security Taxes Payable		2.70
J. C. Allen, Proprietor		13,785.15
	$15,065.38	$15,065.38

J. C. Allen's Post-Closing Trial Balance

PRACTICE ASSIGNMENT No. 20. Complete Report No. 20 in the workbook and submit your working papers to the instructor for approval. You will then be given instructions as to the work to be done next.

Unit Ten

PRACTICAL ACCOUNTING PROBLEMS

The problems in this unit are supplementary to those in the workbook. They are numbered to indicate the unit of the textbook with which they correlate. For example, Problems 1-A and 1-B correlate with Unit One. Loose-leaf stationery should be used in solving these problems. The paper required includes plain ruled paper, two- and four-column journal paper, cash-journal paper, ledger paper, and work sheet paper.

Problem 1-A

O. A. Sargent is a civil engineer. As of December 31 he owned the following property: Cash, $619.12; office equipment, $1,000; and an automobile valued at $1,990. At the same time he owed creditors $280.

REQUIRED: (a) On a basis of the foregoing information, compute the amount of the accounting elements and record them in equation form. (b) Assuming that during the ensuing year there is an increase in Mr. Sargent's assets of $1,400 and a decrease in his liabilities of $30, indicate the changes in the accounting elements by means of an equation.

Problem 1-B

L. J. Radcliffe is an accountant engaged in public practice on his own account. He keeps his accounts on the basis of cash receipts and disbursements. Following is his trial balance taken as of June 30:

TRIAL BALANCE, JUNE 30, 19--

Cash	$ 912.43	
Office Equipment	475.00	
Automobile	1,800.00	
Accounts Payable		$ 231.23
L. J. Radcliffe, Proprietor		2,200.00
L. J. Radcliffe, Drawing	1,500.00	
Income from Professional Fees		3,400.00
Rent Expense	600.00	
Telephone and Telegraph Expense	72.50	
Electric Expense	50.00	
Stationery and Supplies	30.50	
Automobile Expenses	197.20	
Miscellaneous Expenses	53.60	
Charitable Contributions	140.00	
	$5,831.23	$5,831.23

NARRATIVE OF TRANSACTIONS FOR JULY

July 1. (Saturday) Paid one month's rent, $100.
3. Paid electric bill, $7.50.
3. Paid telephone bill, $7.10.
5. Received $275 from a client in payment of services rendered.
7. Paid a garage bill, $21.25.
10. Received $80 from a client in payment of services rendered.
12. Paid Shillito's Department Store, $29.75. (Charge to Mr. Radcliffe's drawing account)
15. Mr. Radcliffe withdrew $125 for personal use.
17. Paid the Underwood Typewriter Co. $75 on account.
19. Received $110 from a client in full for services rendered.
24. Gave the American Red Cross $10.
26. Paid the American Institute of Accountants $25, in payment of annual membership dues.
29. Received $47.50 from a client in payment of professional services.
31. Mr. Radcliffe withdrew $90 for personal use.

REQUIRED: (a) Journalize the July transactions, using standard two-column journal paper. (b) Open the necessary accounts, using the standard account form of ledger paper. Assume each account is kept on a separate page of the ledger and number the accounts consecutively. Record the July 1 balances as shown in the June 30 trial balance, and post the journal entries for July. (c) Foot the ledger accounts, enter the balances, and prove the balances by taking a trial balance as of July 31.

Problem 2-A

Waldo S. May is engaged in business as the sole proprietor of a mercantile establishment. At the end of the current calendar year, the footings of his merchandise accounts appeared as follows:

Merchandise Inventory. Dr. footing, $11,000.
Sales, Cr. footing, $52,248.22.
Sales Returns and Allowances, Dr. footing, $175.
Purchases, Dr. footing, $27,320.
Purchases Returns and Allowances, Cr. footing, $552.

The inventory taken at the end of the year amounted to $7,000.

REQUIRED: Prepare a statement of the gross profit on sales for the year.

Problem 2-B

Samuel E. Oliver is engaged in business as a retail merchant. He keeps a purchases journal, a sales journal, and a two-column general journal as books of original entry. The standard account form of general ledger is used. Individual accounts with customers and creditors are not kept in ledger form; however, the purchase invoices and sales tickets are filed in such a manner that the amounts due to creditors and due from customers may be ascertained at any time. All charge sales are payable by the tenth of the following month. Following is his trial balance taken as of March 31:

SAMUEL E. OLIVER

TRIAL BALANCE, MARCH 31, 19--

Cash	$ 1,109.00	
Accounts Receivable	1,750.00	
Merchandise Inventory	11,000.00	
Store Equipment	580.00	
Accounts Payable		$ 1,894.00
Samuel E. Oliver, Proprietor		4,500.00
Samuel E. Oliver, Drawing	700.00	
Sales		24,400.00
Sales Returns and Allowances	212.50	
Purchases	13,400.00	
Purchases Returns and Allowances		106.00
Rent Expense	450.00	
Advertising Expense	120.00	
Gas and Electric Expense	60.00	
Telephone and Telegraph Expense	36.00	
Wages	1,425.00	
Miscellaneous Expenses	27.50	
Charitable Contributions	30.00	
	$30,900.00	$30,900.00

NARRATIVE OF TRANSACTIONS FOR APRIL

Apr. 1. (Saturday) Paid the rent for April in advance, $150.

3. Paid the following bills:
   Gas and electric bill, $21.50.
   Telephone bill, $10.75.

4. Received invoice No. 71 dated April 1 from C. M. Janis, 124 Spring St., for merchandise purchased, $195. Terms, 30 days net.

4. Sold merchandise on credit to R. A. Stratton, 120 Main St., $26.50. Sale No. 41.

6. Sold merchandise on credit to the Clinton Hotel, 20 Broadway, $80.25. Sale No. 42.

8. Sundry cash sales, $178.

10. Paid the following creditors on account:
   Cramer Bros., $136.50.
   Samuels & Co., $225.40.

11. Received the following remittances from customers to apply on account:
   Sterling Hotel, $75.
   C. L. Woodward, $50.
   Mrs. D. E. Carter, $47.50.

12. Received invoice No. 72 dated April 10 from Harrison & Lang, Detroit, for merchandise purchased, $230. Terms, 30 days net.

Apr. 13. Made credit sales as follows:
No. 43, Mrs. D. E. Carter, Kingston, $84.75.
No. 44, Sterling Hotel, 200 Locust, $52.75.
No. 45, Mrs. O. M. Lawton, 125 E. Fourth St., $60.
14. Paid $27.50 for newspaper advertising.
15. Sundry cash sales, $142.50.
15. Paid semimonthly wages, $237.50.
17. Samuel E. Oliver withdrew $100 for personal use.
18. Made charge sales as follows:
No. 46, L. C. Byrd, 604 Race St., $79.10.
No. 47, Mrs. G. R. Martin, 25 E. Fourth St., $39.10.
No. 48, Clinton Hotel, 20 Broadway, $71.56.
19. Received invoice No. 73 dated April 17 from Cramer Bros., City, for merchandise purchased, $225.40. Terms, 30 days net.
20. Gave the Clinton Hotel credit for $12 on account of merchandise returned.
21. Received credit from Cramer Bros. for $17.80 on account of merchandise returned.
22. Sundry cash sales, $143.70.
24. Received invoice No. 74 dated April 22 from Samuels & Co., Cleveland, for merchandise purchased, $92.50. Terms, 30 days net.
25. Made charge sales as follows:
No. 49, C. L. Woodward, 121 Elm St., $54.40.
No. 50, Sterling Hotel, City, $76.15.
26. Allowed credit for $4.20 to L. C. Byrd for merchandise returned.
27. Paid Davis Bros. $69.50 on account.
27. Received $160 from Clinton Hotel to apply on account.
28. Purchased store equipment on account from the Carew Supply Co., 16 John St., $70. Terms, 60 days net.
28. Paid freight and drayage on merchandise purchased, $18.
29. Sundry cash sales, $156.40.
29. Paid semimonthly wages, $237.50.
29. Samuel E. Oliver withdrew $75 for personal use.

REQUIRED: (a) Journalize the April transactions. Foot the purchases and sales journals, enter the totals, and rule. Prove each page of the general journal by footing the debit and credit columns. (b) Open the necessary general ledger accounts, record the April 1 balances as shown in the March 31 trial balance, complete the individual posting from the general journal, and complete the summary posting from the purchases and sales journals. Foot the accounts and enter the balances in small pencil figures. (c) Take a trial balance. (d) Assuming that an inventory taken on April 30 amounted to $9,400, prepare a statement of the gross profit on sales for the four months' period ending April 30.

Problem 3-A

U. A. Noble is an advertising counselor. His books of original entry include a two-page cashbook and a two-column general journal. He uses the standard account form of general ledger. He keeps his accounts on the basis of cash receipts and disbursements. Following is his trial balance taken as of November 30:

U. A. NOBLE

TRIAL BALANCE, NOVEMBER 30, 19--

Cash	$1,736.14	
Office Equipment	370.00	
Accounts Payable		$ 57.79
U. A. Noble, Proprietor		2,470.00
U. A. Noble, Drawing	2,175.00	
Income from Fees		4,620.00
Rent Expense	825.00	
Telephone and Telegraph Expense	102.50	
Electric Expense	64.75	
Salaries	1,650.00	
Stationery and Supplies	37.50	
Miscellaneous Expenses	41.90	
Charitable Contributions	145.00	
	$7,147.79	$7,147.79

NARRATIVE OF TRANSACTIONS FOR DECEMBER

Dec. 1. (Friday) Paid December office rent in advance, $75.
1. Paid electric bill, $5.42.
2. Paid telephone bill, $9.50.
2. Received a check from Gilmartin Appliance Co. for $150 in payment of services rendered.
4. Received payment from Hughes Mercantile Co. for services rendered, $195.
7. Donated $5 to the American Red Cross.
7. Paid $4.50 for office stationery.
9. Received check for $215 from Laughlin Directory Co. for advertising counsel.
11. Mr. Noble withdrew $150 for personal use.
15. Paid secretary's salary for the half month, $75.
18. Purchased office furniture on credit from Mandel Furniture Co., $300.
19. Paid $2 for having the office windows washed.
20. Received $125 from Walters Provision Co. for services rendered.
22. Paid traveling expenses while on business trip out of city, $17.50.
23. Donated $10 to the Community Chest.
26. Paid Mandel Furniture Co. $50 on account.
28. Mr. Noble withdrew $75 for personal use.
30. Paid secretary's salary for the half month, $75.

REQUIRED: (a) Journalize the December transactions. (b) Open the necessary ledger accounts, record the December 1 balances, and post the cashbook and general journal entries. Balance and rule the cashbook. (c) Take a trial balance.

Problem 3-B

Floyd Powell engages in business as a retail merchant and decides to use the following books of account: (a) purchases journal; (b) sales journal; (c) two-page columnar cashbook; (d) two-column general journal; and (e) loose-leaf general ledger with standard account form of ruling. Merchandise will be sold both for cash and on credit. All credit sales will be due on the tenth of the following month. Individual accounts with customers and creditors will not be kept in ledger form, but the purchase invoices and sales tickets will be filed in such a manner that the amounts due to creditors and due from customers may be ascertained at any time. Following is a chart of the accounts that will be needed in recording the transactions for May:

CHART OF ACCOUNTS

Assets
- Cash
- Accounts Receivable
- Office Equipment
- Store Equipment

Liabilities
- Accounts Payable

Proprietorship
- Floyd Powell, Proprietor
- Floyd Powell, Drawing

Income
- Sales
- Sales Returns and Allowances

Cost
- Purchases
- Purchases Returns and Allowances

Expenses
- Rent Expense
- Advertising Expense
- Delivery Expense
- Telephone Expense
- Salaries
- Charitable Contributions

NARRATIVE OF TRANSACTIONS FOR MAY

May 1. (Monday) Floyd Powell invested $3,500 in a retail merchandising business.
2. Paid one month's rent in advance, $125.
2. Paid $10 to the Bell Telephone Co. for installation and service charge on telephone.
3. Purchased store equipment from the Batesville Furniture Co. on 60 days credit, $340.
4. Received invoice No. 1 dated May 2 from Allison Bros., Kingston, for merchandise purchased, $250. Terms, 30 days.
6. Sold merchandise on credit to R. O. Dale, 31 Race St., $74.50. Sale No. 1.
8. Received invoice No. 2 dated May 4 from The Dalton Mfg. Co., City, for merchandise purchased, $712.60. Terms, 30 days.
9. Paid for newspaper advertising, $17.75.

May 10. Sold merchandise on credit to Mrs. C. A. Walton, Dayton, $54.10. Sale No. 2.
11. Sold merchandise on credit to C. R. Ward, 110 Moorman St., City, $127.50. Sale No. 3.
13. Sundry cash sales, $184.60.
15. Paid semimonthly wages, $105.
15. Mr. Powell withdrew $50 for personal use.
16. Purchased an adding machine for office use from The Acme Sales Co., City, $105. Terms, 60 days.
17. Purchased merchandise for cash from Day Bros., City, $52.50.
18. Sold merchandise on credit to the Brown Cafe, City, $120. Sale No. 4.
19. Received credit for merchandise returned to The Dalton Mfg. Co., $7.59.
20. Sundry cash sales, $186.15.
22. Sold merchandise on credit to Mrs. L. M. Kenton, 40 Park Ave., City, $112.60. Sale No. 5.
23. Received $50 from R. O. Dale on account.
24. Paid Allison Bros. $125 on account.
25. Allowed credit for merchandise returned by Mrs. L. M. Kenton for $12.60.
26. Donated $15 to the Y. M. C. A.
27. Sundry cash sales, $134.50.
29. Received invoice No. 3 dated May 27 from The Acme Electric Co., City, for merchandise purchased, $215.50. Terms, 30 days.
29. Sold merchandise on credit to C. R. Ward, 110 Moorman St., City, $162.75. Sale No. 6.
31. Paid $27.50 for delivery service.
31. Paid semimonthly wages, $105.
31. Mr. Powell withdrew $80 for personal use.

REQUIRED: (a) Journalize the May transactions. Foot the amount columns in the purchases and sales journals, enter the totals, and rule. Foot the amount columns in the cashbook, enter the totals, rule, and record the balance in the Description column below the double rules. (b) Open the necessary general ledger accounts, complete the individual posting from the general journal and cashbook, and complete the summary posting from the purchases journal, sales journal, and cashbook. Foot the accounts and enter the balances in small pencil figures. (c) Take a trial balance. (d) Assuming that an inventory taken on May 31 amounted to $600, prepare a statement of the gross profit on sales for the month of May.

Problem 3-C

J. C. Hilliard engages in the retail clothing business. He uses a purchases journal, a sales journal, an eight-column combined cash-journal, and a general ledger with standard account form of ruling. Merchandise is sold both for cash and on credit, all credit sales being due on the tenth of the following month. Ledger accounts are not kept with individual creditors and customers. Unpaid purchase invoices are filed numerically according to due dates. When paid they are filed alphabetically, under creditors, in another file. Sales tickets are filed alphabetically until payment is received. Following is a chart of accounts kept by Mr. Hilliard:

CHART OF ACCOUNTS

Assets
Cash
Accounts Receivable
Store Equipment

Liabilities
Accounts Payable

Proprietorship
J. C. Hilliard, Proprietor
J. C. Hilliard, Drawing

Income
Sales
Sales Returns and Allowances

Cost
Purchases
Purchases Returns and Allowances

Expenses
Rent Expense
Advertising Expense
Telephone Expense
Salaries
Miscellaneous Expenses

NARRATIVE OF TRANSACTIONS FOR MARCH

Mar. 1. (Wednesday) Mr. Hilliard invested $4,000 cash.
1. Paid one month's rent in advance, $100.
2. Paid $8 for telephone service.
3. Received invoice No. 1 dated March 1 from Kahn Tailoring Co. for merchandise purchased on credit, $275.50.
4. Received invoice No. 2 dated March 2 from Ed. V. Price & Co. for merchandise purchased on credit, $436.50.
4. Sundry cash sales, $320.
6. Sold merchandise on credit to W. W. Griffith, $49.50. Sale No. 1.
7. Sold merchandise on credit to W. H. Gaddis, $92. Sale No. 2.
8. Purchased store equipment from George Tull on credit, $95.
9. Sold merchandise on credit to W. W. Hilligoss, $72. Sale No. 3.
10. Sold merchandise on credit to F. A. Munson, $102. Sale No. 4.
11. Sundry cash sales, $290.
13. Sold merchandise on credit to George Gould, $120. Sale No. 5.
14. Gave W. W. Griffith credit for merchandise returned, $9.
15. Mr. Hilliard withdrew $125 in cash for personal use.
15. Paid salesclerk's semimonthly wages in cash, $70.
16. Received credit for $20 from Kahn Tailoring Co. for merchandise returned by agreement.
17. Paid $22.75 for newspaper advertising.
18. Sundry cash sales, $225.13.
20. Received invoice No. 4 dated March 17 from Goodall Co. for merchandise purchased on credit, $362.50.
21. Paid freight and drayage on merchandise purchased, $12.65.
22. Received $40.50 from W. W. Griffith in payment of the merchandise sold him on March 6.

Mar. 23. Paid George Tull $95 in full for store equipment purchased on March 8.
24. Paid $3 for window washing.
25. Sold merchandise on credit to John Smysor, $122. Sale No. 6.
25. Sundry cash sales, $212.
27. Received $50 from W. W. Hilligoss on account.
27. Purchased a second-hand check protectograph for $20; cash.
28. Paid $21.25 for advertising matter.
28. Received credit for $12.25 from Goodall Co., allowance on defective merchandise.
28. Received invoice No. 5 dated March 23 from M. Born Co. for merchandise purchased on credit, $397.35.
29. Paid Kahn Tailoring Co., $255.50 in full of account.
29. Sold merchandise on credit to J. A. Flint, $69.75. Sale No. 7.
30. Received $75 from W. H. Gaddis on account.
31. Sundry cash sales, $209.
31. Paid salesclerk's semimonthly wages in cash, $70.
31. Mr. Hilliard withdrew $100 in cash for personal use.
31. Paid Ed. V. Price & Co. $436.50 in full of account.

REQUIRED: (a) Journalize the foregoing transactions. Foot, total, and rule the journals. Enter the cash balance in the Description column of the combined cash-journal. (b) Using Mr. Hilliard's chart of accounts as a guide, open the necessary ledger accounts. Complete the individual posting from the combined cash-journal. Complete the summary posting from the purchases journal, sales journal, and combined cash-journal. (c) Take a trial balance as of March 31, using two-column journal paper.

Problem 4-A

M. P. Carroll, a merchant, completed the following transactions with the Harris Trust and Savings Bank during the month of October:

Oct. 2.	(Monday) Balance in bank per record kept on check stubs	$1,900.00	Oct. 11.	Check No. 118....	$ 60.00
			11.	" " 119....	49.50
			13.	" " 120....	457.74
			14.	" " 121....	48.10
2.	Deposit...........	1,000.00	14.	" " 122....	273.42
2.	Check No. 108....	208.80	14.	Deposit...........	341.38
2.	" " 109....	20.00	16.	Check No. 123....	150.00
3.	" " 110....	450.00	18.	" " 124....	256.01
4.	" " 111....	101.00	21.	" " 125....	94.75
5.	" " 112....	150.00	21.	Deposit...........	791.00
6.	" " 113....	75.00	24.	Check No. 126....	141.32
7.	" " 114....	165.50	25.	" " 127....	103.88
7.	" " 115....	40.00	27.	" " 128....	279.77
7.	" " 116....	38.00	28.	" " 129....	38.00
7.	Deposit...........	248.65	30.	" " 130....	567.43
10.	Check No. 117....	445.23	30.	Deposit...........	815.24

REQUIRED: (a) A record of the bank account as it would appear on the check stubs. (b) A reconciliation of the bank statement of November 1 which indicated a balance of $1,667.57 with Checks Nos. 116, 126, 129, and 130 outstanding.

Problem 4-B

William Ellis, a contractor, had a balance of $50 in his petty cash fund as of June 1. During June the following petty cash transactions were completed:

June 2. (Friday) Paid for repairs on a typewriter, $1.25. Voucher No. 44.
6. Paid for carbon paper, $2.95. Voucher No. 45.
8. Donated $5 to the Community Chest fund. Voucher No. 46.
9. Paid garage for washing car, $1. Voucher No. 47.
12. Gave his son, $2. (Charge William Ellis, Drawing) Voucher No. 48.
14. Paid for postage stamps, $3. Voucher No. 49.
17. Paid for newspaper for month, $1.32. Voucher No. 50.
22. Paid for window washing, $2. Voucher No. 51.
27. Paid $1 to the Parent-Teachers Association for dues. (Charge Miscellaneous Expenses) Voucher No. 52.
28. Paid for greasing car, $1. Voucher No. 53.
29. Donated $10 to the American Red Cross. Voucher No. 54.
30. Rendered report of petty cash expenditures for month and received the amount needed to replenish the petty cash fund.

REQUIRED: (a) Record the foregoing transactions in a petty cash disbursements record, distributing the expenditures as follows:

William Ellis, Drawing
Automobile Expenses
Stationery and Supplies
Miscellaneous Expenses
Charitable Contributions

(b) Prove the petty cash disbursements record by footing the amount columns and proving the totals. Enter the totals and rule the amount columns with single and double lines. (c) Prepare a statement of the petty cash disbursements for June. (d) Bring down the balance in the petty cash fund below the ruling in the Description column. Enter the amount received to replenish the fund and record the total amount to be forwarded to the top of a new page for July.

Problem 5-A

L. J. Martin is engaged in business as a furrier. From time to time, notes are accepted from customers to whom furs and fur coats are sold at retail. Notes may also be issued to banks when it is necessary to borrow money for working capital purposes and to creditors from whom furs and fur coats are purchased at wholesale. The following transactions involving notes were selected from the transactions completed during the current year:

NARRATIVE OF TRANSACTIONS

Jan. 15. Borrowed $500 from the Liberty National Bank on a 90-day, 5% interest-bearing note.

Feb. 10. Inasmuch as Donald Rankin's account is past due, his offer to make temporary settlement by paying $74.50 in cash and giving a 60-day, 6% interest-bearing note for the balance amounting to $300, was accepted.

Mar. 20. Sold Mrs. G. R. Robinson a fur coat for $600 receiving $200 in cash and a note for $400 due in 90 days at 6% interest.

April 11. Received a check for $303 from Donald Rankin in payment of his note and interest due today.

April 15. Paid the note due at the Liberty National Bank today; principal, $500; interest, $6.25.

May 18. Purchased furs from The Acme Fur Co. amounting to $2,700, paying $700 in cash and giving a 90-day note with interest at 5% for the balance.

June 18. Mrs. G. R. Robinson called at the office today and paid the interest on her note amounting to $6 and requested an extension of 30 days on the payment of the principal, which was granted.

July 18. Received a check for $402 from Mrs. G. R. Robinson in payment of her note and interest due today.

Aug. 16. Gave The Acme Fur Co. a check for $1,025 in payment of one-half of the principal plus the interest accrued on a note due today, and agreed to pay the balance due on the note in 60 days.

Oct. 15. Gave The Acme Fur Co. a check for $1,008.33 in payment of the balance on note and interest due today.

Nov. 5. Borrowed $600 from the Liberty National Bank giving a 90-day, 5% interest-bearing note.

Nov. 10. Accepted a 60-day, 6% interest-bearing note for $175 from Phillip Koopman in temporary settlement of his account.

REQUIRED: Record the foregoing transactions in general journal form. Foot the amount columns of the journal as a means of proof.

Problem 5-B

L. J. Martin, who is engaged in business as a furrier, occasionally invests surplus funds in securities, including government bonds and corporation bonds and stocks. Following is a narrative of such transactions that were completed during the current year:

NARRATIVE OF TRANSACTIONS

Feb. 1. Cash balance, $9,600.

1. Issued a check for $2,400 in payment of 100 shares of National Acme Co. common stock purchased at $24 a share, including the broker's commission.

Feb. 15. Issued a check for $750 in payment of a $1,000 Series E, U. S. Savings Bond.

Mar. 15. Purchased a $1,000, 2½% U. S. Treasury Bond for $1,000.

May 15. Issued a check for $1,020 in payment of a $1,000 Columbia Electric Co. 3½% bond due in 1960, including the broker's commission; no interest accrued.

July 15. Redeemed a $500, Series E, U. S. Savings Bond at maturity. Original cost $375. (Since Mr. Martin's accounts are kept on the accrual basis, the appreciation in the value of the bond amounting to $125, has already been recorded as interest income.)

Sept. 15. Cashed a $12.50 coupon on a 2½%, $1,000 U. S. Treasury Bond due today.

Nov. 15. Received a check for $17.50 in payment of the semiannual interest on a 3½%, $1,000 Bond of the Columbia Electric Co.

Dec. 15. Received a check for $100 in payment of a dividend at $1 a share on 100 shares of common stock of the National Acme Co.

REQUIRED: Record the foregoing transactions on a sheet of combined cash-journal paper with the following columnar headings:

Cash
- (1) Receipts, Dr.
- (2) Payments, Cr.

General
- (3) Debits
- (4) Credits

Accounts Receivable
- (5) Debits
- (6) Credits

Accounts Payable
- (7) Debits
- (8) Credits

Prove the footings in the usual manner, enter the totals, rule, and bring down the cash balance as of January 1.

Problem 7-A

P. H. O'Brien is engaged in business as a retail electrical supplies dealer. Merchandise is sold for cash and on credit. At the top of the following page is a reproduction of the trial balance columns of his work sheet for the current year ended December 31.

REQUIRED: Prepare a ten-column work sheet making the necessary entries in the Adjustments columns to record the following:

(a) Cost of sales:
  Merchandise inventory, end of year, $6,377

(b) Accruals:
  Interest accrued on notes receivable, $7
  Interest accrued on notes payable, $9.17

(c) Prepaid expenses:
  Prepaid insurance unexpired, $140
  Stationery and supplies on hand, $30

P. H. O'BRIEN
WORK SHEET FOR YEAR ENDED DECEMBER 31, 19--

Accounts	Trial Balance Dr. Balances	Trial Balance Cr. Balances
Cash	2,732.96	
Notes Receivable	700.00	
Accounts Receivable	2,162.00	
Reserve for Bad Debts		24.86
Merchandise Inventory	5,364.00	
Accrued Interest Receivable		
Prepaid Insurance	280.00	
Stationery and Supplies	90.00	
Store Equipment	2,200.00	
Reserve for Depreciation of Store Equipment		220.00
Delivery Equipment	1,800.00	
Reserve for Depreciation of Delivery Equipment		450.00
Notes Payable		1,100.00
Accounts Payable		3,312.10
Employees' Income Taxes Payable		127.50
Social Security Taxes Payable		45.00
Accrued Interest Payable		
P. H. O'Brien, Proprietor		12,666.50
P. H. O'Brien, Drawing	2,000.00	
Sales		25,717.50
Sales Returns and Allowances	89.50	
Interest Income		17.50
Purchases	18,115.65	
Purchases Returns and Allowances		92.15
Rent Expense	1,500.00	
Advertising Expense	450.00	
Salaries	6,000.00	
Social Security Taxes	90.00	
Insurance Expense		
Stationery and Supplies Consumed		
Depreciation Expense		
Loss on Bad Debts		
Miscellaneous Expenses	60.00	
Interest Expense	14.00	
Charitable Contributions	125.00	
Cost of Sales		
	43,773.11	43,773.11

(d) Depreciation:
Store equipment, 10% a year, $220
Delivery equipment, 25% a year, $450

(e) Loss on bad debts:
Increase reserve for bad debts $40 to provide for estimated loss.

Note: Problems 7-B and 8-A are based on P. H. O'Brien's work sheet; hence if those problems are to be solved, the work sheet should be retained for reference until after they are solved, when the solutions of all three probems may be submitted to the instructor.

Problem 7-B

Refer to the work sheet for P. H. O'Brien (based on Problem 7-A) and from it prepare the following financial statements:

(a) A balance sheet in account form as of December 31.

(b) A profit and loss statement for the year ended December 31.

Problem 8-A

Refer to the work sheet for P. H. O'Brien (based on Problem 7-A) and draft the general journal entries required:

(a) To adjust the general ledger accounts so they will be in agreement with the financial statements.

(b) To close the temporary proprietorship accounts on December 31.

Problem 8-B (Complete cycle problem)

R. C. Watson is engaged in a mercantile business on a sole proprietorship basis. He keeps a purchases journal, sales journal, combined cash-journal, and general ledger. For his combined cash-journal, he uses standard eight-column paper with headings arranged as follows:

Cash
- (1) Receipts, Dr.
- (2) Payments, Cr.

General
- (3) Debits
- (4) Credits

Accounts Receivable
- (5) Debits
- (6) Credits

Accounts Payable
- (7) Debits
- (8) Credits

The standard account form of ledger ruling is used. Individual accounts with customers and creditors are not kept in ledger form; however, the purchase invoices and sales tickets are filed in such a manner that the amounts due to creditors and due from customers can be ascertained at any time. At the end of the eleventh month of the current year, his trial balance appeared as shown on the following page.

NARRATIVE OF TRANSACTIONS FOR DECEMBER

Dec. 1. (Friday) Purchased merchandise from Evans Bros., Clinton, $650. Invoice No. 31, dated November 30. Terms, 2/10, n/30.

2. Paid the December rent, $300. Check No. 64.

2. Paid the telephone bill, $13.50. Check No. 65.

2. Sundry cash sales, $153.

4. Paid J. R. Miller $721.50 in full of December 1 balance. Check No. 66.

R. C. WATSON

TRIAL BALANCE, NOVEMBER 30, 19--

Cash	$ 5,139.50	
Notes Receivable	1,800.00	
Accounts Receivable	2,739.90	
Reserve for Bad Debts		$ 69.60
Merchandise Inventory	20,800.00	
Prepaid Insurance	475.00	
Stationery and Supplies	80.00	
Store Equipment	1,900.00	
Reserve for Depr. of Store Equipment		380.00
Notes Payable		1,200.00
Accounts Payable		1,768.00
Employees' Income Taxes Payable		122.50
Social Security Taxes Payable		133.50
R. C. Watson, Proprietor		31,900.00
R. C. Watson, Drawing	3,700.00	
Sales		83,680.00
Sales Returns and Allowances	126.40	
Purchases Discount		110.00
Interest Income		9.00
Purchases	63,200.00	
Purchases Returns and Allowances		141.10
Rent Expense	3,300.00	
Advertising Expense	2,400.00	
Salaries and Commissions	12,900.00	
Social Security Taxes	580.50	
Miscellaneous Expenses	183.40	
Interest Expense	14.00	
Charitable Contributions	175.00	
	$119,513.70	$119,513.70

Dec. 5. Sold merchandise on credit to A. F. Wade, 32 Main St., City, $350. Sale No. 101.

6. Purchased merchandise from the Dixon Supply Co., Maryville, $975. Invoice No. 32, dated December 5. Terms, 30 days.

7. Received $175 from Russell Long in full payment of his account.

8. Paid Evans Bros. $637 in settlement of their invoice of November 30, less 2% discount. Check No. 67.

8. Received $208 from H. L. Beck in full payment of his account.

9. Sold merchandise on credit to C. A. Jordan, Dayton, $241.50. Sale No. 102.

9. Sundry cash sales, $498.

11. Purchased merchandise from the Campbell Mfg. Co., City, $1,621.90. Invoice No. 33, dated December 9. Terms, 30 days.

12. Sold merchandise on credit to R. E. Keith, 201 King St., City, $325.70. Sale No. 103.

Dec. 13. Issued Check No. 68 to the Second National Bank, a U. S. Depositary, in payment of the following taxes:

(a) Employees' income taxes withheld during November		$122.50
(b) Social security taxes imposed for old-age and survivors' insurance benefits —		
On employees (withheld during November)	$17.20	
On the employer	17.20	34.40
Total		$156.90

14. Sold merchandise on credit to D. R. Brown, 738 High St., City, $625. Sale No. 104.

15. Issued Check No. 69 payable to Pay Roll for $515.96.

PAYROLL STATEMENT FOR PERIOD ENDED DECEMBER 15

Total wages and commissions earned during period		$586.00
Employees' taxes to be withheld:		
(a) For employees' income taxes	$61.25	
(b) For old-age and survivors' insurance benefits @ 1½%	8.79	70.04
Net amount payable to employees		$515.96
Employer's payroll taxes:		
(a) For old-age and survivors' insurance benefits @ 1½%		$8.79
(b) For unemployment compensation benefits —		
State @ 2.7%	$15.82	
Federal (3% less state contributions of 2.7%)	1.76	17.58
Total		$ 26.37

(In addition to recording the amounts withheld from employees' wages for income tax purposes and for old-age and survivors' insurance benefits, the social security taxes imposed on the employer should also be recorded.)

16. Sundry cash sales, $515.30.
18. R. C. Watson withdrew $60 for personal use. Check No. 70.
19. Gave R. E. Keith credit for $20 because a part of the merchandise sold him on the twelfth was returned.
20. Sold merchandise on credit to A. F. Wade, 32 Main St., $212.50. Sale No. 105.
21. Purchased merchandise from the White Mfg. Co., City, $1,487.25. Invoice No. 34, dated December 20. Terms, 30 days.
22. Received $305.70 from R. E. Keith in full of Sale No. 103.
23. Paid bill for advertising, $115. Check No. 71.
23. Sundry cash sales, $385.15.
26. Sold merchandise on credit to L. D. Marvin, 159 Jackson St., City, $735. Sale No. 106.
26. Purchased merchandise from Evans Bros., Clinton, $975.40. Invoice No. 35, dated December 23. Terms, 2/10, n/30.
26. Received a check for $200 from A. F. Wade to apply on account.

Dec. 27. Sold merchandise on credit to R. E. Keith, 201 King St., City, $362.75. Sale No. 107.

27. Sent the Campbell Mfg. Co. a check for $500 to apply on account. Check No. 72.

28. Sold merchandise on credit to S. T. Gross, 218 Seventh St., City, $913.45. Sale No. 108.

28. Purchased store equipment from the Centerville Supply Co., Centerville, $210. Terms, 60 days net.

29. Received $241.50 from C. A. Jordan in payment of Sale No. 102.

29. Received credit from Evans Bros. for $45 because a part of the merchandise purchased on the twenty-sixth was returned by agreement.

29. Sold merchandise on credit to C. A. Jordan, Dayton, $487.10. Sale No. 109.

30. Sundry cash sales, $495.75.

30. Issued Check No. 73 payable to Pay Roll for $541.27.

PAYROLL STATEMENT FOR PERIOD ENDED DECEMBER 31

Total wages and commissions earned during period		$615.00
Employees' taxes to be withheld:		
(a) For employees' income taxes	$64.50	
(b) For old-age and survivors' insurance benefits @ 1½%	9.23	73.73
Net amount payable to employees		$541.27
Employer's payroll taxes:		
(a) For old-age and survivors' insurance benefits @ 1½%		$ 9.23
(b) For unemployment compensation benefits —		
State @ 2.7%	$16.61	
Federal (3% less state contributions of 2.7%)	1.84	18.45
Total		$ 27.68

REQUIRED: (a) Journalize the December transactions. (b) Open the necessary general ledger accounts, and record the December 1 balances, using the November 30 trial balance as the source of the needed information. Complete the individual and summary posting from the books of original entry. (c) Take a trial balance of the general ledger accounts. (d) Prepare a ten-column work sheet making the required adjustments for the following:

(1) Cost of sales:

Merchandise inventory, end of year, $33,700

(2) Accruals:

Interest accrued on notes receivable, $24

Interest accrued on notes payable, $12

(3) Prepaid Expenses:
Prepaid insurance unexpired, $317
Stationery and supplies on hand, $25
(4) Depreciation:
Store equipment, 10% a year, $190
(5) Loss on bad debts:
Increase reserve for bad debts, $105.68, to provide for estimated loss.

In recording the required adjustments on the work sheet, it will be necessary to add the following account titles to those already appearing in the trial balance:

Accrued Interest Receivable
Accrued Interest Payable
Insurance Expense
Stationery and Supplies Consumed
Depreciation Expense
Loss on Bad Debts
Cost of Sales

(e) Prepare a balance sheet in report form as of December 31 and a profit and loss statement for the year ending December 31. (f) Record the adjusting entries in the combined cash-journal and post. (g) Record the closing entries in the combined cash-journal and post. (h) Balance and rule the accounts that are in balance after the adjusting and closing entries have been posted; also balance and rule the cash account, and rule the merchandise inventory account. (i) Take a post-closing trial balance.

Problem 9-A

Dr. William Krummel is a surgeon. He keeps his accounts on the cash basis, using a combined cash-journal and a general ledger as his principal books of account. For his combined cash-journal, he uses standard eight-column paper with headings arranged as follows:

Cash
(1) Receipts, Dr.
(2) Payments, Cr.

General
(3) Debits
(4) Credits

Professional Fees
(5) Cash Service, Cr.
(6) Patients' Accts., Cr.

Wage Deductions
(7) Employees' Income Taxes Payable, Cr.
(8) S. S. Taxes Payable, Cr.

Dr. Krummel has two employees as follows:

Mary Brammel, nurse. Semimonthly salary, $100. Deductions: (a) $1.50 for old-age and survivors' insurance benefits; (b) $8.20 for federal income taxes.

Lillian Randall, secretary. Semimonthly salary, $80. Deductions: (a) $1.20 for old-age and survivors' insurance benefits; (b) $9.60 for federal income taxes.

Since Dr. Krummel has less than eight employees, he is not subject to the federal tax imposed for unemployment compensation purposes. Neither is he required to make contributions to a state unemployment compensation fund because he is located in a state that does not require contributions of employers of less than eight employees.

All professional expenses applicable to the office are charged to Office Expenses. These include rent, electricity, telephone and telegraph expense, janitor service, laundry, etc.

From time to time, Dr. Krummel invests his surplus funds in real and personal property. In addition to the account titles given in the headings of the combined cash-journal, the following accounts will be affected in recording the transactions that were completed during the month of August:

Government Bonds	Mortgages Payable
Corporation Bonds	Interest Received
Corporation Stocks	Dividends Received
Notes Receivable	Interest Paid
Lot 1416 Sycamore St.	Salaries
Building — Paxton Sub.	Gain on Government Bonds
Notes Payable	Gain on Real Estate

NARRATIVE OF TRANSACTIONS FOR AUGUST

Aug. 1. (Tuesday) Cash balance, $12,450.
3. Paid office rent for August in advance, $125.
4. Paid telephone bill, $14.50.
5. Paid electric bill, $17.25.
7. Received $300 from Mrs. J. B. Thornton in payment of statement rendered for professional fees.
8. Purchased a $100 U. S. Savings Bond for $75.
10. Received a check for $20 in payment of a quarterly dividend of 40 cents a share on 50 shares of Kroger Grocery & Baking Co. common stock.
14. Received $400 from H. B. Brand in payment of statement rendered for professional fees.
15. Purchased one $1,000 Bell Telephone of Pennsylvania, 5% Bond, for $1,205, including brokers' commission; no interest accrued.
15. Paid the semimonthly salaries of the nurse and secretary, withholding the proper amounts for old-age and survivors' insurance benefits and employees' income taxes.
16. Sold one $1,000 U. S. Treasury, $2\frac{7}{8}$% Bond, receiving $1,090 after deducting the brokers' commission. (Dr. Krummel had purchased this bond at the issue price of $1,000.)

Aug. 17. Dependable Building Co. completed the construction of a house on Dr. Krummel's Lot 43, Paxton Subdivision. Contract price $21,500. Paid $11,000 down and executed a mortgage for $10,500 in favor of Dependable Building Co.

18. Received from John Duncan a check for $1,500 in payment of lot located at 1416 Sycamore St. (Original cost, $1,200)

19. Paid note due today at the Liberty National Bank. Principal, $750; interest, $15.

21. Received $15 in cash in payment of consultation fees.

22. Received $430 in payment of a note; principal, $400; interest, $30.

23. Paid the Industrial Savings Bank $202.07 to release Lot 43, Paxton Subdivision from the mortgage held on the lot. Principal, $200; interest, $2.07.

28. Purchased 50 shares of Standard Oil Co. common stock for $1,400, including brokers' commission.

31. Paid the semimonthly salaries of the nurse and secretary, withholding the proper amounts for old-age and survivors' insurance benefits and employees' income taxes.

REQUIRED: (a) Record the foregoing transactions using a sheet of combined cash-journal paper. (b) Foot the amount columns, prove the footings, record the totals, and rule the combined cash-journal.

Problem 9-B

Carl Smith is an architect engaged in professional practice on his own account. Since his income consists entirely of compensation for personal services rendered, he keeps his accounts on the cash basis. His trial balance for the current year ending December 31 is as follows:

CARL SMITH

TRIAL BALANCE, DECEMBER 31, 19--

Cash	$ 1,917.53	
Office Equipment	960.00	
Reserve for Depr. of Office Equipment		$ 96.00
Automobile	1,820.00	
Reserve for Depr. of Automobile		227.50
Accounts Payable		380.26
Employees' Income Taxes Payable		42.60
Social Security Taxes Payable		13.50
Carl Smith, Proprietor		2,864.20
Carl Smith, Drawing	4,250.00	
Income from Professional Fees		8,959.49
Rent Expense	1,200.00	
Salaries	1,800.00	
Automobile Expenses	212.00	
Social Security Taxes	27.00	
Miscellaneous Expenses	277.02	
Charitable Contributions	120.00	
	$12,583.55	$12,583.55

REQUIRED: (a) Prepare a ten-column work sheet making the necessary entries in the Adjustments columns to record the depreciation of the following assets:

Office Equipment, 10%, $96.
Automobile, 25%, $455.

(b) Prepare the following financial statements:

(1) A balance sheet in report form as of December 31.

(2) A profit and loss statement for the year ended December 31.

Problem 9-C

Lee Reynolds owns and operates a theatrical booking agency. His fixed assets include office equipment and an automobile that is used for business purposes only. The reserve method is used in accounting for depreciation. In preparing a work sheet for the year ended December 31, his bookkeeper made adjustments thereon for the following:

	COST	RATE OF DEPRECIATION
(a) Office equipment..................	$2,600	10% a year
(b) Automobile........................	$1,800	25% a year

REQUIRED: Using journal ruled paper, draft the adjusting entries required to bring the general ledger accounts into agreement with the financial statements.

Problem 9-D

Joseph P. Darius operates a real estate agency and keeps his accounts on the cash basis. A reproduction of the Profit and Loss columns of his work sheet for the current year ended December 31 appears on the following page.

REQUIRED: (a) Using journal ruled paper, draft the entries required (1) to close the income and expense accounts into the profit and loss summary account and (2) to close the profit and loss summary account, assuming that Mr. Darius had withdrawn $2,400 during the year for personal use and that he desired to have the balance of his net income transferred to his permanent capital account.

(b) Open an account with Profit and Loss Summary, No. 33, and post the closing entries to it. Be sure to itemize the accounts that are transferred to the profit and loss summary account and, after completing the posting, rule the account.

JOSEPH P. DARIUS

WORK SHEET FOR YEAR ENDED DECEMBER 31, 19--

Accounts	Acct. Nos.	Profit and Loss Dr. Balances	Profit and Loss Cr. Balances
Income from Commissions	41		8,788.95
Interest Received	42		14.50
Rent Expense	51	1,020.00	
Tel. and Tel. Expense	52	76.50	
Salaries	53	1,680.00	
Automobile Expenses	54	482.75	
Stationery and Supplies	55	96.30	
Depreciation Expense	56	41.25	
Social Security Taxes	57	25.20	
Miscellaneous Expenses	58	53.94	
Charitable Contributions	59	95.00	
		3,570.94	8,803.45
Net Income		5,232.51	
		8,803.45	8,803.45

Problem 9-E

Fred Bullock operates an airline charter service, specializing in day and night airplane service. Following is a trial balance of his general ledger accounts taken as of December 31:

FRED BULLOCK

TRIAL BALANCE, DECEMBER 31, 19--

Cash	$ 5,982.23	
Office Equipment	1,250.00	
Reserve for Depreciation of Office Equipment		$ 250.00
Airplane Equipment	59,600.00	
Reserve for Depreciation of Airplane Equip.		23,840.00
Notes Payable		1,200.00
Accounts Payable		1,500.50
Employees' Income Taxes Payable		200.00
Social Security Taxes Payable		30.00
Fred Bullock, Proprietor		21,500.00
Fred Bullock, Drawing	4,200.00	
Traffic Income		42,781.26
Rent Expense	2,800.00	
Salaries	8,000.00	
Office Expense	700.00	
Airplane Expense	8,495.13	
Social Security Taxes	120.00	
Miscellaneous Expenses	54.40	
Charitable Contributions	100.00	
	$91,301.76	$91,301.76

REQUIRED: (a) Prepare a ten-column work sheet making the necessary adjustments to record the depreciation of fixed assets as follows:

PROPERTY	RATE OF DEPRECIATION	AMOUNT OF DEPRECIATION
Office equipment	10%	$ 125
Airplane equipment	20%	11,920

(b) Prepare a balance sheet in report form as of December 31. (c) Prepare a profit and loss statement for the year ended December 31. (d) Draft the general journal entries required:

(1) To adjust the general ledger accounts so that they will be in agreement with the financial statements.

(2) To close the temporary proprietorship accounts on December 31, assuming that Mr. Bullock desires to have a sufficient amount of the net income transferred to his drawing account to balance the account and the remainder transferred to his capital account.

Problem 9-F

Isaac Miller is the sole proprietor of a dry cleaning establishment. Since his income consists of compensation for services rendered, he keeps his accounts on the cash basis. He does not extend credit to customers but operates on a cash-on-delivery basis. The Trial Balance columns of his work sheet for the current year ended December 31 are reproduced on the following page.

(a) Complete the work sheet making the necessary adjusting entries to record the depreciation of fixed assets as follows:

Office equipment, 10% a year, $50
Cleaning equipment, 8% a year, $144
Delivery truck, 30% a year, $276

(b) Prepare a balance sheet as of December 31 in report form and a profit and loss statement for the year ending December 31.

(c) Using combined cash-journal paper, draft the adjusting and closing entries required to bring the general ledger accounts of Mr. Miller into agreement with his financial statements. Foot the amount columns of the combined cash-journal and prove the footings.

ISAAC MILLER

Work Sheet for Year Ended December 31, 19--

Accounts	Trial Balance Dr. Balances	Trial Balance Cr. Balances
Security National Bank	3,156.40	
Office Equipment	500.00	
Reserve for Depreciation of Office Equipment		50.00
Cleaning Equipment	1,800.00	
Reserve for Depreciation of Cleaning Equipment		144.00
Delivery Truck	920.00	
Reserve for Depreciation of Delivery Truck		276.00
Accounts Payable		205.34
Employees' Income Taxes Payable		112.10
Social Security Taxes Payable		15.42
Isaac Miller, Proprietor		3,808.22
Isaac Miller, Drawing	3,162.45	
Dry Cleaning Income		9,308.85
Pressing Income		3,989.51
Rent Expense	2,080.00	
Salaries	4,112.50	
Delivery Expense	414.43	
Depreciation Expense		
Miscellaneous Expenses	398.30	
Social Security Taxes	61.69	
Heat, Light, and Power	1,303.67	
	17,909.44	17,909.44

Part II

INTERMEDIATE ACCOUNTING

ACCOUNTING FOR PROPRIETORSHIP

XXI THE SOLE PROPRIETORSHIP

Proprietorship is a term commonly used in referring to the ownership of an enterprise. Ownership or proprietorship of an enterprise may be vested in one individual, in two or more partners, or in a group of stockholders, depending upon the legal organization of the enterprise. If an enterprise is owned by one individual, it is known as a sole proprietorship; if owned by two or more partners, it is known as a partnership; if owned by a group of stockholders, it is known as a corporation.

In small mercantile enterprises and in personal service enterprises the sole proprietorship form of organization predominates. The medical and dental professions, for example, are composed largely of individuals who are engaged in practice as sole proprietors. One reason for the popularity of the sole proprietorship form of organization is that it is easily organized, involving no formal or legal agreement with others as to ownership or conduct. Anyone may engage in a lawful enterprise merely by complying with state and local laws.

Organization of a Sole Proprietorship. When engaging in an enterprise as a sole proprietor, an individual decides the amount he will invest and the nature of the property to be invested. The original investment may consist of cash only, or of cash and any other property that is owned, such as merchandise, office equipment, store equipment, and delivery equipment. The property invested is usually segregated from any other property that may be owned by the proprietor. An individual may engage in more that one enterprise and may operate each separately as a sole proprietorship. In such cases, it is preferable to keep separate records of the activities of each enterprise.

In comparison with other forms of business organization, the sole proprietorship offers certain advantages, such as the following:

(a) Simplicity of organization.
(b) Freedom of initiative and industry.
(c) Fewer required government reports.
(d) Strong incentive to individual enterprise.

There are some disadvantages in the sole proprietorship form of organization, of which the following are most significant:

(a) The amount of available capital may be limited.
(b) The amount of credit may be restricted.
(c) The proprietor is solely responsible for all debts incurred.

Accounting Procedure. In general, the accounting procedure in recording the ordinary operating transactions of an enterprise is not affected by the type of organization. Whether an enterprise is operated as a sole proprietorship by an individual, as a partnership by two or more partners, or as a corporation by stockholders through directors and officers has little bearing on the accounting procedure in recording the routine transactions arising from the ordinary operations of the business. However, the required proprietorship accounts depend largely upon the type of organization.

Proprietorship Accounts. Proprietorship accounts may be subdivided into two groups as follows:

(a) Temporary proprietorship accounts.
(b) Permanent proprietorship accounts.

The temporary proprietorship accounts are those in which increases and decreases in proprietorship arising from the transactions completed during an accounting period are recorded. Such accounts are also known as profit and loss accounts or income and expense accounts. At the end of the fiscal period they are closed by transferring their balances to a profit and loss summary account.

The profit and loss summary account is a clearing account that generally is used only in the closing process at the end of the accounting period. The temporary proprietorship accounts are closed by transferring their balances to the profit and loss summary account.

The proprietor's personal or drawing account is also a temporary account that is usually closed at the end of each accounting period. If the net income for the period exceeds the amount withdrawn by the proprietor during the period, the drawing account may be closed by transferring to it a sufficient amount of the net income from the profit and loss summary account. If the business has been operated at a profit but the net income amounts to less than the amount withdrawn during the period, the entire net income should be transferred from the profit and loss summary account to the proprietor's drawing account and the drawing account should then be closed by transferring its balance to the proprietor's capital account. If the business has been operated at a loss, the balances of both the profit and loss summary account and the proprietor's drawing account should be transferred to the proprietor's capital account, after which the profit and loss summary account and the drawing account will be in balance and should be ruled.

In a sole proprietorship the proprietor's capital account is the only permanent proprietorship account. The balance of this account represents the amount of the proprietor's investment in the enterprise. After all the accounts are closed, the balance of the proprietor's capital account is usually brought down below the ruling as his *present capital.*

Opening Entries. An individual may invest cash and other property in a sole proprietorship enterprise. Certain liabilities may attach to the property invested. If the investment consists solely of cash, the opening entry will involve a debit to Cash or the bank account and a credit to the proprietor's capital account for the amount invested.

If cash and other property such as office equipment, store equipment, or other equipment are invested, the opening entry will involve a debit to Cash or the bank account for the amount of cash invested, debits to appropriate equipment accounts for the value of the other property invested, and a credit to the proprietor's capital account for the total amount of the investment.

If, at the time of organizing an enterprise, there are any liabilities such as accounts payable, notes payable, or mortgages payable applicable to the property invested, appropriate accounts representing the liabilities should be credited and the proprietor's capital account should be credited only for the excess of the value of the assets invested over the aggregate amount of the liabilities. In other words, the proprietor's capital account should be credited for his *equity* in the assets invested.

EXAMPLE: J. A. Bryant decides to engage in a mercantile business and invests cash amounting to $4,500, office equipment valued at $600, store equipment valued at $400, and delivery equipment valued at $900. He owes $200 on the office equipment, and there is a mortgage outstanding amounting to $400 on the delivery equipment. The opening entry in general journal form to record Bryant's investment is as follows:

Bank	$4,500.00	
Office Equipment	600.00	
Store Equipment	400.00	
Delivery Equipment	900.00	
Accounts Payable		$ 200.00
Mortgage Payable		400.00
J. A. Bryant, Proprietor		5,800.00
Investment in business.		

(The bank account is debited for the amount of cash invested for the reason that it is the usual custom of business firms to deposit all cash receipts in the bank and to make all disbursements by check. Under this plan a cash account is not kept in the general ledger. Instead, all receipts are debited to the bank account and all disbursements are credited to the bank account. This method of accounting for cash is followed consistently throughout this treatise. It should be understood, however, that a cash account and one or more bank accounts may be kept in the general ledger, if desired.)

To install a new set of books for a going enterprise operated as a sole proprietorship, the opening entry may be journalized and posted to the general ledger accounts. The principles involved are the same as in opening the books for a new enterprise, except that the balances of any reserve accounts should be recorded as credits to the proper accounts. Before opening the new books, financial statements should be prepared and the old books should be closed. The balance sheet and the schedules of accounts receivable and accounts payable will then provide the information needed in opening the new books.

EXAMPLE: J. A. Bryant, after operating for a period of five years, decided to install a new set of books. Financial statements were prepared and the old books were closed in the usual manner. The balance sheet prepared at that time appeared as follows:

J. A. BRYANT

BALANCE SHEET, DECEMBER 31, 19--

Assets			Liabilities	
Cash		$ 4,750.00	Notes Payable	$ 1,000.00
Accounts Rec.	$3,800.00		Accounts Payable	3,200.00
Less Res. for Bad Debts	400.00	3,400.00	Total Liabilities	$ 4,200.00
Merchandise Inventory		6,950.00		
Office Equip.	$1,600.00		**Proprietorship**	
Less Res. for Depr.	400.00	1,200.00	J. A. Bryant, Proprietor	14,300.00
Store Equip.	$1,200.00			
Less Res. for Depr.	300.00	900.00		
Delivery Equip.	$1,900.00			
Less Res. for Depr.	600.00	1,300.00		
Total Assets		$18,500.00	Total Liabilities and Proprietorship	$18,500.00

The opening entry in general journal form to open the new books is as follows:

Bank	$4,750.00	
Accounts Receivable	3,800.00	
Merchandise Inventory	6,950.00	
Office Equipment	1,600.00	
Store Equipment	1,200.00	
Delivery Equipment	1,900.00	
Notes Payable		$ 1,000.00
Accounts Payable		3,200.00
Reserve for Bad Debts		400.00
Reserve for Depr. of Office Equipment		400.00
Reserve for Depr. of Store Equipment		300.00
Reserve for Depr. of Delivery Equipment		600.00
J. A. Bryant, Proprietor		14,300.00
Opening a new set of books.		

After opening the necessary accounts in the general ledger, the opening journal entry should be posted in the usual manner. Entering the balances of the accounts with customers in the accounts receivable ledger may be done directly from a schedule of accounts receivable. Entering the balances of the accounts with creditors in the accounts payable ledger may be done directly from a schedule of accounts payable.

Proprietary Transactions Completed During the Accounting Period. Certain types of transactions may be referred to as proprietary transactions because they affect either the proprietor's drawing account or his capital account. The following are typical proprietary transactions:

(a) Cash withdrawn by proprietor for personal use.
(b) Proprietor's personal or family expenditures.
(c) Withdrawal of capital by proprietor.
(d) Additional capital contributed by proprietor.

Cash withdrawn periodically by the proprietor for personal use is usually charged to his personal or drawing account on the theory that such amounts represent withdrawals in anticipation of profits. Such withdrawals are sometimes regarded as salary or compensation for personal services rendered; however, they represent charges to the proprietor's personal or drawing account and should not be treated as an operating expense of the enterprise.

Personal and family expenditures should also be charged to the proprietor's personal or drawing account. The payment of personal or family bills or accounts from funds of the enterprise are expenditures of this type. It is not unusual for an individual engaged in an enterprise as a sole proprietor to pay all personal and family or household bills by issuing checks against the same bank account as that used for business expenditures of the enterprise. However, care should be used in recording all checks issued, and those representing personal or family expenditures should be charged to the proprietor's personal or drawing account, while those representing business expenditures should be charged to the proper expense, asset, or liability accounts.

A sole proprietor may, at any time, withdraw a portion of the capital invested in his business or he may contribute additional capital in the form of cash or other property. Withdrawals, representing decreases in the capital invested, should be charged to his capital account; additional investments should be credited to his capital account.

Distribution of Net Income or Net Loss at End of Accounting Period. It is customary to close the temporary proprietorship accounts at the end of each accounting period, which may be either a calendar year or a fiscal year. As the temporary accounts are closed, their balances are transferred to a profit and loss summary account. After all of the temporary proprietorship accounts have been closed into the profit and loss summary account, the difference between the footings of the account will represent the amount of the net income or the net loss for the year. If the account has a credit balance, it will represent net income; if the account has a debit balance, it will represent net loss.

The distribution of any net income should be in accordance with the proprietor's instructions. These instructions may vary as indicated by the following discussion:

(a) The proprietor may prefer to have a sufficient amount of his net income transferred to his drawing account in order to balance that account and the remainder transferred to his capital account as an addition to his investment in the enterprise.

(b) The proprietor may prefer to have all of the net income transferred to his drawing account, with a view to withdrawing it at some future time, instead of leaving it in the business as a permanent addition to his capital.

(c) The proprietor may prefer to have transferred to his drawing account an amount equal to the total previously withdrawn, plus an additional amount to be withdrawn immediately in cash, with an understanding that the balance of the net income is to be left in the business as an addition to his capital.

(d) The proprietor may be undecided as to what to do with the net income; hence he may give instructions to transfer to his drawing account an amount sufficient to balance that account and to leave the remainder in the profit and loss summary account until he decides whether to withdraw it or to leave it in the business as an addition to his capital.

Usually a sufficient amount of the net income is transferred to the proprietor's personal or drawing account in order to balance the account and the remaining net income is transferred to the proprietor's capital account. The profit and loss summary account and the drawing account are then in balance and should be ruled in the usual manner. The proprietor's capital account should also be balanced and ruled, and the balance should be brought down below the ruling on the credit side.

If the proprietor elects to have all of the net income transferred to his drawing account, it is only necessary to debit the profit and loss summary account and to credit the proprietor's drawing account for the amount of the net income, after which the profit and loss summary account will be in balance and should be ruled. The proprietor's capital account will have a credit balance. His drawing account will also have a credit balance if the net income exceeds the total amount previously charged to his drawing account. The credit balance of his capital account represents his permanent investment in the enterprise, while the credit balance of his drawing account represents a temporary investment that may be withdrawn at any time.

If the proprietor elects to withdraw a part of the net income in cash and to leave the balance in the business as an addition to his capital, it is advisable to transfer to his drawing account an amount equal to the debit balance of the drawing account plus the additional amount to be withdrawn immediately. For example, if the proprietor's drawing account has a debit balance of $3,600 at the end of an accounting period and he decides to withdraw an additional $1,000 of his net income in cash, a total of $4,600 should be transferred from the profit and loss summary account to the drawing account and the remainder of the net income should be transferred to the proprietor's capital account. To record the withdrawal of $1,000, it will then only be necessary to debit the drawing account and to credit the bank account for $1,000, after which the drawing account will be in balance. Under this plan, the proprietor's drawing account provides a complete record of all withdrawals by the proprietor.

If the proprietor is undecided as to the disposition of the net income in excess of the withdrawals, an amount sufficient to balance the drawing account may be transferred from the profit and loss summary account.

The credit balance of the profit and loss summary account will then represent the undistributed income of the enterprise. Usually the account is balanced and ruled and the balance is brought down below the ruling on the credit side.

If a business is operated at a net loss, the profit and loss summary account will have a debit balance after all the temporary accounts are closed at the end of the accounting period. A net loss represents a decrease in proprietorship; hence the profit and loss summary account should be closed by transferring the net loss to the proprietor's capital account. If the proprietor has made withdrawals for personal use during the period, the debit balance of his drawing account should also be transferred to his capital account in order that the balance of his capital account will represent his net worth at the end of the period.

Proprietary Accounts in the Balance Sheet. The method of exhibiting the proprietary interest of the owner in the balance sheet of a sole proprietorship is shown on pages 206, 207, and 260. There may be some variation in the account titles used by different enterprises; however, the final results should be the same since the balance sheet is an exhibit of the accounting elements, including (a) the assets, (b) the liabilities, and (c) the proprietorship. The accounts in the proprietorship section of the balance sheet should be arranged to show the proprietor's capital at the beginning of the accounting period, the net increase or the net decrease in his capital during the period, and his present capital or net worth at the end of the period.

PRACTICE ASSIGNMENT No. 21. Complete Report No. 21 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 22 is required.

XXII THE PARTNERSHIP

When two or more individuals engage in an enterprise as co-owners the organization is known as a partnership. This form of organization is prevalent in practically all types of enterprises; however, it is more popular among personal service enterprises than among mercantile enterprises. For example, the partnership form of organization is quite common in the legal and public accounting professions.

Organization of a Partnership. The Uniform Partnership Act stipulates that "a partnership is an association of two or more persons who carry on, as co-owners, a business for profit." The partners may, by agreement, unite their capital, labor, skill, or experience in the conduct of a business for their mutual benefit. While under certain circumstances a partnership may be formed by means of an oral or an implied agreement, it is desirable that a partnership agreement be evidenced by a written contract. Such a contract is known as *articles of copartnership.* There is no standard form of partnership agreement, but there are certain provisions that are uniformly desirable, such as the following:

(a) Date.
(b) Names of the partners.
(c) Nature of the business.
(d) Duration of the agreement.
(e) Name and location of the firm.
(f) Investment of each partner.
(g) Basis on which profits or losses are to be shared by the partners.
(h) Accounting methods.
(i) Limitation of partners' rights.
(j) Salary allowances.
(k) Duties of partners.
(l) Unusual restraints upon the partners.
(m) Division of assets upon dissolution of the partnership.
(n) Signatures of the partners.

The articles of copartnership reproduced in Illustration No. 26 constitute a partnership agreement drawn in the usual form.

The partnership form of organization offers advantages similar to those of the sole proprietorship. Additional advantages include the following:

(a) The ability and the experience of the partners are combined in one enterprise.
(b) More capital may be raised because the resources of the partners are combined.
(c) Credit may be improved because each partner is personally liable for partnership debts.

There are some disadvantages that are peculiar to the partnership form of organization, including the following:

(a) Each partner is individually liable for all the debts of the partnership. The liability of each partner is not limited to a pro rata share of the partnership debts; he is personally liable for all debts of the partnership to the same extent as if he were the sole proprietor. Under the laws of some states, certain partners may limit their liability; at least one partner, however, must be a general partner who is responsible for all the debts of the partnership.

(Continued on page 303)

ARTICLES OF COPARTNERSHIP

This Contract, *Made and entered into on the* first *day of* July *19*— *by and between* J. A. Bryant, of Chicago, Illinois, Party of the First Part, and W. L. Wood, of the same city and state, Party of the Second Part,

WITNESSETH: That the said parties have this day formed a copartnership for the purpose of engaging in and conducting a wholesale auto accessories *business under the following stipulations which are made a part of this contract:*

FIRST: The said copartnership is to continue for a term of twenty-five years *from date hereof.*

SECOND: The business shall be conducted under the firm name of Bryant & Wood

THIRD: The investments are as follows: Each partner, $15,000 in cash

FOURTH: All profits or losses arising from said business are to be shared as follows: Equally

FIFTH: A systematic record of all transactions is to be kept in a double entry set of books, which are to be open for the inspection of each partner. The accounts are to be kept on the accrual basis.

On June 30 of each year *hereafter a statement of the business is to be made, the books closed and each partner credited with his share of the gain. A statement may be made at such other time as the partners agree upon.*

SIXTH: Each partner is to devote his entire time and attention to the business and to engage in no other business enterprise without the written consent of the other.

*SEVENTH: Each partner is to receive a salary of $*400.00 *per month, the same to be treated as an operating expense in computing net profit. Neither partner is to withdraw from the business an amount in excess of his salary without the written consent of the other.*

EIGHTH: The duties of each partner are defined as follows: J. A. Bryant as senior partner is to act as general manager and to have general supervision of the business. W. L. Wood is to serve as purchasing agent and sales manager, with supervision of the merchandise stock. Each partner is to attend to such other duties as are deemed necessary for the successful operation of the business.

NINTH: Neither partner is to become surety or bondsman for anyone without the written consent of the other.

TENTH: In case of death, incapacity, or withdrawal of either partner, the business is to be conducted for the remainder of the fiscal year by the surviving partner, and the profits for the year allocated to the withdrawing partner to be determined by the ratio of the time he was a partner during the year to the whole year.

ELEVENTH: In case of dissolution, the assets are to be divided between the partners in the ratio of the capital invested at the time of dissolution.

IN WITNESS WHEREOF, The parties aforesaid have hereunto set their hands and affixed their seals on the day and year above written.

J. A. Bryant

W. L. Wood

Illustration No. 26, Articles of Copartnership

(b) A partner cannot transfer his interest in the partnership without the consent of the other partners.
(c) Termination of the partnership agreement, bankruptcy of the firm, or death of one of the partners dissolves the partnership.

Accounting Procedure. In accounting for the operations of a partnership, it is necessary to keep a separate capital account for each partner. It is also customary to keep a separate personal or drawing account for each partner. While no new principles are involved in keeping these accounts, care should be used in drafting the opening entry and in recording any transactions thereafter that affect the respective interests of the partners.

Opening Entries. When two or more individuals engage in an enterprise as partners, each may invest cash and other property. Certain liabilities may be assumed by the partnership, such as accounts payable, notes payable, and mortgages payable. In opening the books for a partnership, it is customary to draft a separate journal entry to record the investment of each partner. The proper asset accounts should be debited for the amounts invested, the proper liability accounts should be credited for the amounts assumed, and the partner's capital account should be credited for his equity in the assets. The opening entries for Bryant & Wood based on the articles of copartnership reproduced in Illustration No. 26 may be made in general journal form as follows:

Bank	$15,000.00	
J. A. Bryant, Partner		$15,000.00
J. A. Bryant invested $15,000 in cash.		
Bank	$15,000.00	
W. L. Wood, Partner		$15,000.00
W. L. Wood invested $15,000 in cash.		

If, instead of investing $15,000 in cash, Bryant were to invest office equipment valued at $600 on which he owes $200, delivery equipment valued at $900 on which he owes $400 represented by a mortgage, and $14,100 in cash, the proper opening entry in general journal form to record his investment would be as follows:

Bank	$14,100.00	
Office Equipment	600.00	
Delivery Equipment	900.00	
Accounts Payable		$ 200.00
Mortgage Payable		400.00
J. A. Bryant, Partner		15,000.00
J. A. Bryant's investment in partnership.		

Sometimes two or more individuals who have been engaged in business as sole proprietors form a partnership for the purpose of combining their businesses. Their respective balance sheets are the basis for the opening entries to record the investments of such partners. For example, on April 1, C. E. Palmer and A. G. Sawyer form a partnership under the firm name of Palmer & Sawyer to continue the conduct of the businesses they have been operating as sole proprietors. They agree to invest the assets shown in their respective balance sheets. It is also agreed that the partnership shall assume the liabilities shown in their respective balance sheets. Each partner is to receive credit for his equity in the assets invested by him, and the profits and losses are to be shared on the basis of Palmer, two fifths, and Sawyer, three fifths. In case of dissolution, the assets are to be distributed between the partners on the basis of their respective capital ratios at the time of dissolution. The balance sheets reproduced below were made a part of the partnership agreement.

C. E. PALMER
BALANCE SHEET, MARCH 31, 19--

ASSETS			LIABILITIES	
Cash		$ 1,033.00	Notes Payable	$ 1,000.00
Accounts Rec.	$1,771.32		Accounts Payable	3,231.60
Less Res. for Bad Debts	137.52	1,633.80	Total Liabilities	$ 4,231.60
Mdse. Inventory		6,875.86	PROPRIETORSHIP	
Store Equip.	$1,200.00		C. E. Palmer, Proprietor	6,192.06
Less Res. for Depr.	319.00	881.00		
Total Assets		$10,423.66	Total Liabilities and Proprietorship	$10,423.66

A. G. SAWYER
BALANCE SHEET, MARCH 31, 19--

ASSETS			LIABILITIES	
Cash		$ 1,136.30	Notes Payable	$ 2,000.00
Accounts Rec.	$1,700.00		Accounts Payable	3,243.00
Less Res. for Bad Debts	200.00	1,500.00	Total Liabilities	$ 5,243.00
Mdse. Inventory		9,517.22	PROPRIETORSHIP	
Supplies		91.90	A. G. Sawyer, Proprietor	8,702.42
Office Equip.	$ 800.00			
Less Res. for Depr.	200.00	600.00		
Store Equip.	$1,500.00			
Less Res. for Depr.	400.00	1,100.00		
Total Assets		$13,945.42	Total Liabilities and Proprietorship	$13,945.42

Since the partnership is taking over the fixed assets at their book value, the cost of such property should be adjusted for prior accumulated depreciation up to the date of the transfer. Thus, the cost of the store equipment contributed by Palmer should be adjusted for the depreciation accumulated prior to the organization of the partnership. The adjusted value is the difference between the cost of $1,200 and the accumulated depreciation of $319, or $881. Likewise, the cost of the office equipment and the store equipment contributed by Sawyer should be adjusted for the depreciation accumulated prior to the organization of the partnership. The adjusted value of the office equipment is $600 and the store equipment $1,100.

The proper entries in general journal form to record the partners' investments are as follows:

April 1.	Bank	$1,033.00	
	Accounts Receivable	1,771.32	
	Merchandise Inventory	6,875.86	
	Store Equipment	881.00	
	Notes Payable		$1,000.00
	Accounts Payable		3,231.60
	Reserve for Bad Debts		137.52
	C. E. Palmer, Partner		6,192.06
	C. E. Palmer's investment in partnership.		
1.	Bank	$1,136.30	
	Accounts Receivable	1,700.00	
	Merchandise Inventory	9,517.22	
	Supplies	91.90	
	Office Equipment	600.00	
	Store Equipment	1,100.00	
	Notes Payable		$2,000.00
	Accounts Payable		3,243.00
	Reserve for Bad Debts		200.00
	A. G. Sawyer, Partner		8,702.42
	A. G. Sawyer's investment in partnership.		

Had the fixed assets of Palmer and Sawyer been taken over by the partnership at any value other than their book value, the assets should be recorded in the books of the partnership at the value agreed upon. For example, if it had been agreed that the store equipment invested by Palmer was to be valued at $1,000 instead of its book value, Store Equipment should be debited for $1,000 instead of $881. Thus, the book value of the store equipment as shown in Palmer's balance sheet of March 31 would be ignored and the store equipment would be recorded in the books of the partnership at the value agreed upon between the partners. Such agreed value represents the cost of the store equipment to the partnership.

It will be observed that the ratio of the partners' investments in the partnership is not exactly the same as their profit and loss sharing ratio. The basis on which profits and losses are to be shared is a matter of agreement between the partners and it is not necessarily the same as their investment ratio. It should be recognized that there are factors other than capital invested that may enter into a profit and loss sharing agreement. For example, one partner may contribute most of the capital but may render no services, while the other partner may contribute less capital but may devote his full time to the partnership; therefore, they may agree to share the profits equally.

Admitting a New Partner. A new partner may be admitted to a partnership by agreement among the partners. For example, Palmer and Sawyer may admit W. H. Walker as a partner and agree to share profits and losses on the basis of their capital ratio. If his investment consisted of cash only, the proper entry to admit him to the partnership would involve a debit to the bank account and a credit to his capital account for the amount invested. If Walker has been operating a business of his own as a sole proprietor and his business is taken over by the partnership, his balance sheet will serve as a basis for drafting the opening entry. Assume that, as of July 1, Walker was admitted to the partnership. The assets listed in his balance sheet are taken over, his liabilities are assumed, and he is given credit for his equity in the assets. His balance sheet follows:

W. H. WALKER

BALANCE SHEET, JUNE 30, 19--

Assets			Liabilities	
Cash		$ 2,865.46	Notes Payable	$ 2,900.00
Accounts Rec.	$4,580.00		Accounts Payable	2,419.65
Less Res. for Bad Debts	345.43	4,234.57	Total Liabilities	$ 5,319.65
Mdse. Inventory		7,747.25	**Proprietorship**	
			W. H. Walker, Proprietor	9,527.63
Total Assets		$14,847.28	Total Liabilities and Proprietorship	$14,847.28

The proper entry in general journal form to admit Walker as a partner is shown at the top of the following page.

July 1.	Bank	$2,865.46	
	Accounts Receivable	4,580.00	
	Merchandise Inventory	7,747.25	
	Notes Payable		$2,900.00
	Accounts Payable		2,419.65
	Reserve for Bad Debts		345.43
	W. H. Walker, Partner		9,527.63
	W. H. Walker admitted to partnership.		

The admission of a new partner calls for the dissolution of the old partnership and the creation of a new partnership. A new partnership agreement should be drawn covering all the usual provisions.

Goodwill. Some business organizations are able to earn consistently profits that are very large in relation to the amount of the recorded assets that they possess. This excess earning power may be due to exceptional management, good location, or one or more of several other factors. When such a condition exists, the business is said to possess *goodwill.* Because of the fact that goodwill is difficult to measure and may not be permanent, accountants do not favor its formal recognition as an asset unless it has been purchased.

For example, suppose that Palmer and Sawyer purchased the business of W. H. Walker for $12,134.54 cash, acquiring all his business assets except cash and assuming all his liabilities. If the book value ($11,981.82) of the assets purchased from Walker was considered to be their fair value, Palmer and Sawyer paid $5,472.37 more for the business than the net value of the assets acquired. This amount may be considered to be the price paid for the goodwill of Walker's business. The transaction could be recorded as follows:

July 1.	Accounts Receivable	$4,580.00	
	Merchandise Inventory	7,747.25	
	Goodwill	5,472.37	
	Notes Payable		$ 2,900.00
	Accounts Payable		2,419.65
	Reserve for Bad Debts		345.43
	Bank		12,134.54
	Purchased W. H. Walker's business.		

It is permissible to record goodwill if a new partner is taken into a firm and is allowed a capital interest in excess of the net assets he invests. For example, suppose that, instead of purchasing Walker's business, Palmer and Sawyer had agreed to take him into the firm as a partner and to give him a capital interest of $15,000 for his business (including his business cash.) Walker's investment might be recorded as follows:

July 1.	Bank	$2,865.46	
	Accounts Receivable	4,580.00	
	Merchandise Inventory	7,747.25	
	Goodwill	5,472.37	
	Notes Payable		$ 2,900.00
	Accounts Payable		2,419.65
	Reserve for Bad Debts		345.43
	W. H. Walker, Partner		15,000.00
	W. H. Walker admitted to partnership.		

Goodwill is considered to be an *intangible asset.* When goodwill is recorded in the accounts, it is usually reported in the balance sheet as the last item in the asset section.

Compensation of Partners. The compensation of partners may be in the form of salaries, royalties, commissions, bonuses, or other compensation. The amount of each partner's compensation and the method of accounting for it should be stated in the partnership agreement. For example, in the articles of copartnership shown in Illustration No. 26, it is stipulated that each partner is to receive a salary of $400 a month. When all partners receive the same salaries and when profits and losses are shared equally, it is immaterial whether the salaries are treated as an expense of the partnership or as withdrawals of anticipated profits. Under the federal income tax law, salaries or other compensation paid to partners for services rendered may not be claimed as a deduction from gross income in the income tax return of the partnership. However, the partnership agreement may provide that partners' salaries are to be treated as an operating expense in computing the net income or the net loss to be shared by the partners.

If partners' salaries are not treated as an expense of the partnership, it is not necessary to keep a salary account for each partner. Amounts withdrawn by the partners as compensation for services may simply be charged to their respective drawing accounts. If partners' salaries are treated as an operating expense, it is usually advisable to keep a separate salary account for each partner. For example, the salaries specified in the partnership agreement between J. A. Bryant and W. L. Wood are to be treated as an operating expense. If the salaries are paid regularly, such as monthly or semimonthly, it will be necessary only to debit each partner's salary account and to credit the bank account. Instead of paying partners' salaries regularly in cash, they may be credited to the partners' drawing accounts. The partners may then draw against such salaries at will.

Under this plan the proper entry to record each partner's salary on each payday is to debit his salary account and to credit his drawing account for the proper amount.

Distribution of Partnership Profits and Losses. The partnership agreement should specify the basis on which profits and losses are to be shared by the partners. In the absence of an agreement between the partners, profits and losses must be shared equally regardless of the ratio of the partners' investments. If the partnership agreement specifies how profits are to be shared, but does not specify how losses are to be shared, the losses must be shared on the same basis as that indicated for the profits.

After closing the temporary accounts into the profit and loss summary account at the end of the accounting period, the balance will represent either net income or net loss. If the account has a credit balance, it represents net income; if the account has a debit balance, it represents net loss.

The distribution of any net income should be in accordance with the partnership agreement. Usually each partner's share of the net income is transferred to his drawing account and he is permitted to withdraw it at will. Should the partners agree to leave a portion of the income in the business as additional capital, the amount so treated should be transferred to the partners' capital accounts. The procedure in distributing the net income or the net loss of a partnership at the close of each accounting period is similar to that of a sole proprietorship except that the income or the loss is divided between the partners on the basis of their agreement. In the absence of an agreement, such income or loss must be shared equally.

Dissolution of a Partnership. As previously explained, dissolution of a partnership may be brought about through bankruptcy or the death of one of the partners. A partner cannot retire from the partnership before its termination without the consent of his partners. To do so would constitute a violation of the partnership agreement and would make him liable to his partners for any loss resulting from his retirement.

By agreement, a partner may retire and be permitted to withdraw assets equal to or more or less than the amount of his proprietary interest in the partnership. The book value of a partner's interest is shown by the credit balance of his capital account after all profits or losses have been distributed in accordance with the agreement and the books are closed. Should the retiring partner withdraw cash or other assets equal to the credit balance of his capital account, the transaction will have no effect upon the capital of the remaining partners.

Suppose, for example, that sometime after W. H. Walker had been taken into the partnership of Palmer and Sawyer, he expressed a desire to retire and his partners agreed to his withdrawal of cash equal to the amount of his equity in the assets of the partnership. After closing the temporary proprietorship accounts into the profit and loss summary account and after distributing the profits and closing the partners' drawing accounts, the partners' capital accounts had credit balances as follows:

C. E. Palmer	$ 7,000.00
A. G. Sawyer	9,000.00
W. H. Walker	10,000.00

This indicates that the book value of Walker's interest in the partnership amounts to $10,000. If this amount is withdrawn in cash, the entry in general journal form to record the transaction in the books of the partnership is as follows:

W. H. Walker, Partner	$10,000.00	
Bank		$10,000.00
W. H. Walker retired, withdrawing $10,000 in settlement of his equity.		

While the transaction involves a decrease in the asset cash with a corresponding decrease in the aggregate capital of the partnership, it does not affect the equity of the remaining partners. Thus, Palmer still has an equity of $7,000 and Sawyer $9,000 in the partnership assets.

If a partner agrees to withdraw less than the book value of his interest in the partnership, the effect of the transaction will be to increase the capital accounts of the remaining partners. To record such a transaction it is necessary to debit the retiring partner's account for the amount of its credit balance, to credit the assets withdrawn, and to credit the remaining partners' accounts for the difference between the value of the assets withdrawn and the credit balance of the retiring partner's account.

Thus, if Walker had agreed to withdraw only $8,000 in settlement for his equity in the assets of the partnership, the transaction should be recorded in the books of the partnership as follows:

W. H. Walker, Partner	$10,000.00	
Bank		$8,000.00
C. E. Palmer, Partner		875.00
A. G. Sawyer, Partner		1,125.00
W. H. Walker retired, withdrawing $8,000 in settlement of his equity.		

The difference between Walker's equity in the assets of the partnership and the amount of cash withdrawn is $2,000. This difference is divided between the remaining partners on a basis of their profit and loss sharing agreement which happens to be the same as their capital ratio. Thus, Palmer is credited for 7/16 of $2,000, or $875, while Sawyer is credited for 9/16 of $2,000, or $1,125.

If a partner is permitted to withdraw more than the book value of his interest in the partnership, the effect of the transaction is to decrease the capital accounts of the remaining partners. Thus, if Palmer and Sawyer had agreed to Walker's withdrawal of $12,000 in settlement for his equity in the assets of the partnership, the transaction should be recorded in the books of the partnership as follows:

W. H. Walker, Partner	$10,000.00	
C. E. Palmer, Partner	875.00	
A. G. Sawyer, Partner	1,125.00	
Bank		$12,000.00
W. H. Walker retired, withdrawing $12,000 in settlement of his equity.		

The excess of the amount of cash withdrawn over Walker's equity in the partnership is divided between the remaining partners on a basis of their profit and loss sharing agreement. Thus, Palmer is debited for 7/16 of $2,000, or $875, while Sawyer is debited for 9/16 of $2,000, or $1,125.

When a partner retires from the business his interest may be purchased by one or more of the remaining partners or by an outside party. If he sells his interest to one of the remaining partners his equity is merely transferred to the other partner. Thus if instead of withdrawing cash in settlement of his equity in the partnership, Walker sells his interest to Palmer, the only entry required to record the transaction on the books of the partnership is as follows:

W. H. Walker, Partner	$10,000.00	
C. E. Palmer, Partner		$10,000.00
C. E. Palmer purchased W. H. Walker's interest in the partnership.		

It is immaterial as to the amount paid Walker for his interest. Any profit or loss resulting from the transaction is a personal gain or loss affecting the individual parties to the transaction but not the firm. If Walker should sell his interest to an outside party who is admitted to the partnership, the only entry needed to record the transaction is an entry to transfer Walker's interest to the new partner. Thus, a journal entry should be made debiting Walker's capital account and crediting the capital account of the new partner for $10,000. It is immaterial as to the price paid Walker for his interest. The transaction is a personal one between the individuals concerned and any gain or loss involved is of no concern to the partnership.

Partnership Accounts in the Balance Sheet. The method of exhibiting the proprietary interests of the partners in the balance sheet of a partnership is similar to that of a sole proprietorship except that the proprietary interest of each partner should be shown separately. The usual arrangement of the proprietorship section of the balance sheet for a partnership is as follows:

PROPRIETORSHIP

J. A. Bryant, Proprietorship, January 1, 19--.....		$6,483.40		
Net Income (½ of $3,779.40).........	$1,889.70			
Less Withdrawals................	1,126.60	763.10		
Proprietorship, December 31, 19--.............			$7,246.50	
W. L. Wood, Proprietorship, January 1, 19--....		$6,602.40		
Net Income (½ of $3,779.40)........	$1,889.70			
Less Withdrawals.................	1,127.35	762.35		
Proprietorship, December 31, 19--.............			7,364.75	
Total Proprietorship.......................				$14,611.25

The net income that is distributed to the partners is the net income computed in accordance with the partnership agreement.

PRACTICE ASSIGNMENT No. 22. Complete Report No. 22 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 23 is required.

XXIII THE CORPORATION

A private corporation is an artificial person created by law for an expressed purpose, combining the capital of its stockholders for their mutual benefit. It differs from a sole proprietorship or from a partnership from the standpoints of organization, ownership, and distribution of profits.

Organization of a Corporation. To incorporate an enterprise, a charter must be obtained from the state in which the corporation is to be formed.

The persons who file application for a charter or for a certificate of incorporation are known as the *incorporators*. Such persons must be competent to contract, some or all must be citizens of the state in which the application is filed, and usually each incorporator is required to be a subscriber for one or more shares of the capital stock. The incorporators must all sign the application for the charter.

The procedure in incorporating an enterprise must conform to the laws of the state in which it is desired to incorporate. The laws of the different states vary considerably in their provisions relating to the organization of corporations. Persons desiring to incorporate a company should acquaint themselves with the laws of the state in which they wish to incorporate, as it will be necessary to comply with the laws of that state. The following excerpts from the laws of one of the states will illustrate the procedure to be observed in forming a corporation:

"Private corporations may be created by the voluntary association of three or more persons for the purposes authorized by law and in the manner hereinafter mentioned.

"A charter must be prepared, setting forth:

1. The name of the corporation;
2. The purpose for which it is formed;
3. The place or places where the business is to be transacted;
4. The term for which it is to exist;
5. The number of directors or trustees, and the names and residences of those who are appointees for the first year; and
6. The amount of the capital stock, if any, and the number of shares into which it is divided.

"It must be subscribed by three or more persons, two of whom must be citizens of this State, and must be acknowledged by them, before an officer duly authorized to take acknowledgments of deeds.

"The certificate of incorporation shall also set forth the minimum amount of capital with which the corporation will commence business, which shall not be less than $1,000. The certificate of incorporation may also contain any provision which the incorporators may choose to insert for the management of the business and for the conduct of the affairs of the corporation, and any provisions creating, defining, limiting, and regulating the powers of the corporation, the directors and the stockholders, or any class of the stockholders.

"The affidavit of those who executed the charter shall be furnished to the Secretary of State, showing:

1. The name, residence, and post-office address of each subscriber to the capital stock of such company;
2. The amount subscribed by each, and the amount paid by each;
3. The cash value of any property received, with its description, location, and from whom and the price at which it was received; and
4. The amount, character, and value of labor done, and from whom and the price at which it was received."

The Charter. After articles of incorporation or a petition for a charter has been filed, and other conditions, such as the payment of incorporation fees, have been fulfilled, the document is examined by a court or an administrative officer. If the instrument is satisfactory and the other requirements have been met, a license, a certificate of incorporation, or a charter is issued and recorded or filed as required by the particular statute of the state concerned. In Illustration No. 27 is shown a charter issued to a corporation under the laws of the state of Texas. While, as previously stated, the provisions of law governing corporation organization vary in different states, in general they include all the important factors peculiar to a corporation, such as name, purpose, duration, location, and capitalization.

Ownership of a Corporation. Ownership of a corporation is represented by capital stock, and the owners of the stock are known as *stockholders.*

Subscriptions to the capital stock of a corporation may be made before or after incorporation. A subscription made before incorporation is an agreement to subscribe for stock. It is a contract entered into between the subscriber and the incorporator or promoter and not between the subscriber and the corporation. The corporation, as such, does not exist until after articles of incorporation have been filed with the secretary of state or other proper official. A subscription to capital stock after incorporation is a contract between the subscriber and the corporation.

Stockholders. All parties holding stock of a corporation, or whose subscriptions for stock have been accepted, are known as stockholders. In order to possess all of the rights of a stockholder of record, the party holding stock must have his ownership duly recorded in the books of the issuing company. If a party purchases stock from a stockholder, such stock must be transferred in the books of the issuing company before the purchaser is entitled to have a certificate of stock in his own name, to vote, or to share in any dividends declared.

Directors. The stockholders elect a *board of directors* that is charged with the management and direction of corporate affairs. It will readily be seen that it would be impracticable for all the stockholders of a large corporation to meet periodically or at special times to decide upon questions in connection with the direction and management of affairs; hence, the stockholders elect a board of directors that is responsible to the stockholders for the proper management of the corporate affairs. The directors are held to be the agents of the corporation.

A board of directors usually consists of three or more stockholders. Where the board is composed of a large number of persons, it is customary

(Continued on page 316)

THE STATE OF TEXAS }
COUNTY OF DALLAS } *KNOW ALL MEN BY THESE PRESENTS:*

That we, the subscribers hereto, citizens of the State of Texas, under the provisions of the Revised Statutes of the State of Texas, do hereby form and incorporate ourselves into a voluntary association and corporation to transact a mercantile business and particularly to purchase and sell goods, wares, and merchandise used for said business, having all the authority, express or implied, by the Statutes of the State of Texas, and to that end we do hereby adopt and subscribe the following, to-wit:

CHARTER

Article 1. This corporation shall be named and known as THE BRYANT COMPANY, INC., by which name it shall contract and be contracted with, sue and be sued, and transact all other business.

Article 2. This corporation is formed for the purpose of transacting a mercantile business and particularly to purchase and sell goods, wares, and merchandise usually offered for sale by wholesale and retail merchants engaged in such business.

Article 3. The place of business of this corporation shall be Dallas County, Texas, the principal office being at Dallas in Dallas County, Texas, and said corporation having the right, power, and authority to operate and do business anywhere in the State of Texas.

Article 4. Said corporation shall exist for a term of fifty years.

Article 5. The business of this corporation shall be transacted by not less than three and not more than twenty-one directors, who shall be elected by the stockholders annually on the last Tuesday of July, the following named stockholders being hereby declared to be directors for the first year:

J. A. BRYANT
W. L. WOOD
RICHARD SMITH

Article 6. The capital stock of this corporation shall consist of five hundred (500) shares with a par value of One Hundred Dollars ($100) each, all common voting stock, all of which has been in good faith subscribed, and one half thereof has been paid for in cash, as shown by affidavit hereto attached.

Article 7. This corporation when created reserves to itself, and for and on behalf of its stockholders, all rights, powers, and privileges granted by the laws of the State of Texas at this time, with the right to accept all laws hereafter passed granting additional powers.

IN TESTIMONY WHEREOF, witness our signatures this 28th day of June, A. D. 19--.

(*Signed*) J. A. BRYANT
W. L. WOOD
RICHARD SMITH

THE STATE OF TEXAS }
COUNTY OF DALLAS }

BEFORE ME, the undersigned authority, a Notary Public in and for Dallas County, Texas, on this day personally appeared J. A. Bryant, W. L. Wood, and Richard Smith, all known to me to be the persons whose names are subscribed to the foregoing instrument and acknowledged to me that they each executed the same for the purposes and consideration therein expressed.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this 28th day of June, A. D. 19--.

(*Signed*) ALLEN JONES
Notary Public in and for
Dallas County, Texas

Illustration No. 27, Charter of a Corporation

to appoint an *executive committee* of from three to five members of the board, who are given authority to administer the affairs of the corporation.

Officers. The board of directors elects the officers. Usually a president, vice-president, secretary, and treasurer are elected as executive officers. One person often holds two positions; for instance, one person may serve both as secretary and treasurer. All the officers are responsible to the board of directors and receive their instructions from the board. They have no authority whatever other than to perform the duties imposed by the by-laws of the corporation and the statutes of the state. Generally they are liable for fraud or misrepresentation, or for exceeding the rights and powers conferred by the by-laws of the company or the statutes of the state.

Capital Stock. The charter obtained by a corporation specifies the amount of capital stock that it is authorized to issue. The state authorizes a corporation to issue a certain number of shares of stock, and it is illegal for a company to issue a greater number of shares than is authorized in its charter. In Illustration No. 28 is shown a certificate of stock issued to J. A. Bryant by The Bryant Company, Inc., with the stub completed. It will be noted that the stub of the stock certificate book provides information as to the number of shares issued and the date of issue.

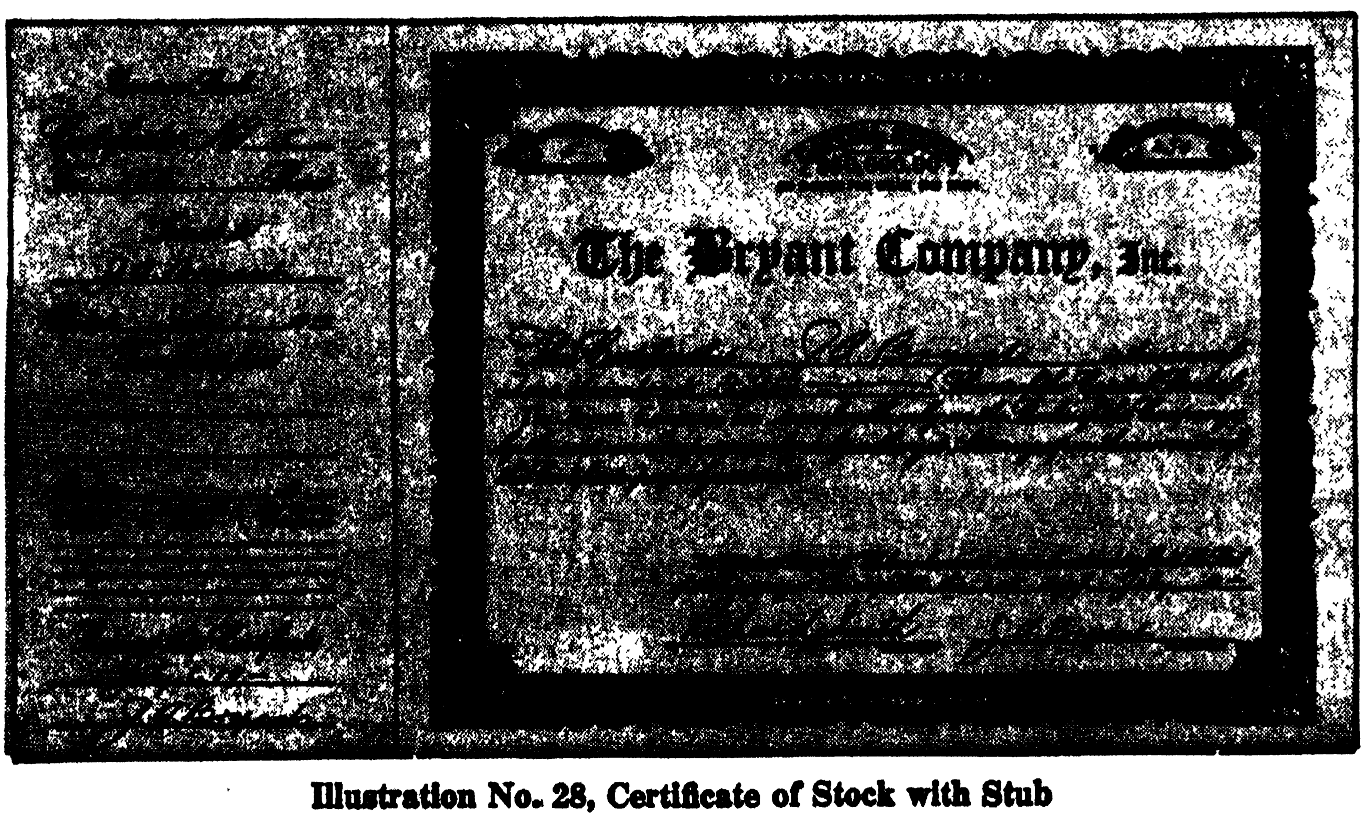


Illustration No. 28, Certificate of Stock with Stub

Different classes of capital stock may be issued, such as common stock and preferred stock. The stock may or may not have par value. Stock that is evidence of ordinary ownership in a corporation is known as common stock. If a certain class of stock is given preference over another class, it is known as preferred stock. Capital stock may be preferred as to assets or dividends, or both. Usually preferred stock is preferred as to dividends. This means that the preferred stockholders are entitled to receive dividends at a specified rate before the common stockholders may share in the profits.

Authorized capital stock that has not been issued is known as *unissued stock*. It has no asset value and should not be treated as an asset. The difference between the amount of the authorized capital stock and the amount of the unissued capital stock represents the amount of the stock issued and outstanding.

The total book value of the capital stock issued by a corporation represents the capital of the company. The book value of the stock is the par or stated value of the capital stock outstanding, plus the amount of any *surplus* or less the amount of any *deficit*. When the total capital of a corporation exceeds the par or stated value of the capital stock, the excess represents surplus. The term surplus is sometimes referred to as earnings retained in the business. When the total capital of a corporation is less than the par or stated value of the stock, the difference represents a deficit.

The book value of each share of capital stock outstanding may be found by dividing the total book value of any class of stock by the number of shares issued. Where both common stock and preferred stock have been issued, the par or redemption value of the preferred stock should be deducted from the total book value of all stock to find the book value of the common stock.

The book value of capital stock may differ from either the par value or the market value. In fact, it is seldom that these values will be identical. The par value or stated value of capital stock is an arbitrary value placed upon the shares issued, while the market value is the value at which the shares may be bought and sold. Where capital stock is listed on an exchange and is actively traded in, the market value may be readily ascertained. Where the stock is not listed on an exchange and is seldom traded in, it may be difficult to ascertain the true market value, because the market value of a share of stock is the price it will command in the open market when offered for sale.

Corporate Transactions. The ordinary operating transactions of a corporation are similar to those of a sole proprietorship or of a partnership operating a business of like nature. Corporate transactions are those involving capital stock or those that affect the interest of the stockholders in some way. Following are a few typical corporate transactions:

(a) Capital stock subscriptions.
(b) Payments received to apply on capital stock subscriptions.
(c) Issuing of capital stock to subscribers.
(d) Transfer of capital stock from one stockholder to another stockholder.
(e) Declaration and payment of dividends.

Corporate Accounts. Following is a list of account titles that are peculiar to the corporate form of organization:

ACCOUNT TITLES	CLASSIFICATION
Unissued Capital Stock	Capital
Authorized Capital Stock	Capital
Subscriptions Receivable	Asset
Capital Stock Subscribed	Capital
Surplus	Capital
Dividends Payable	Liability

Before any stock has been issued, the debit balance of the unissued capital stock account and the credit balance of the authorized capital stock account should be the same. If the capital stock has par value, the amount of these balances will represent the par value of the total stock authorized by the charter. If the capital stock does not have par value, the balances of these accounts will represent the stated value placed on the capital stock authorized by the charter.

For example, if, prior to the issuance of any stock, the unissued capital stock and the authorized capital stock accounts have balances amounting to $50,000 and under the charter the corporation is authorized to issue 500 shares of capital stock, the par value or stated value of each share would amount to $100.

After a part of the authorized capital stock has been issued, the difference between the debit balance of the unissued capital stock account and the credit balance of the authorized capital stock account will represent the par or stated value of the capital stock issued.

For example, after 100 shares of the capital stock referred to in the preceding example are issued, the authorized capital stock account will have a credit balance of $50,000 while the unissued capital stock account will have a debit balance of only $40,000. The difference, $10,000, represents the par or stated value of the stock issued. Since 100 shares were issued, their par or stated value must have amounted to $100 a share.

The subscriptions receivable account will have a debit balance until the subscribers have paid in the entire amount subscribed. The debit balance of this account represents an asset the same as any other receivable account.

The capital stock subscribed account will have a credit balance until certificates for all of the stock subscribed have been issued to the subscribers. After all subscriptions are paid in full and certificates of stock have been issued to all subscribers, the account will be in balance.

The surplus account is a capital account to which the undistributed profits of a corporation are usually credited. In the sole proprietorship and partnership forms of organization, any profits left in the business usually are credited to the capital accounts of the proprietors; in a corporation, undistributed profits are never credited to the capital stock accounts but are credited to the surplus account.

Dividends Payable is a liability account the same as any other payable account. A decision on the part of the directors of a corporation to pay a dividend is commonly referred to as a *declaration of dividends*. When dividends are declared and such dividends are payable at a later date, it is customary to record the declaration by debiting Surplus and by crediting Dividends Payable. The dividends payable account will have a credit balance until all dividends declared have been paid in full, after which the account will be in balance. When dividends are paid immediately upon being declared, there is no need for setting up an account with Dividends Payable. Usually the dividends are paid sometime after being declared by the directors, and in the meantime the amount of the dividends declared represents a liability of the corporation that should be listed in the balance sheet as Dividends Payable.

Accounting Procedure. Following is a narrative of corporate transactions with illustrative journal entries:

(1) The Bryant Company, Inc. was incorporated with an authorized issue of 500 shares of common capital stock, par value $100 per share. At the time of incorporation, subscriptions had been received as follows:

J. A. Bryant	250 shares
W. L. Wood	125 shares
Richard Smith	125 shares

The stock was subscribed for at par value and one half of the subscription price was paid in cash, the balance to be paid on demand.

To record this transaction it is necessary (a) to record the authorized issue of stock, (b) to record the stock subscriptions received, and (c) to record the cash received to apply on the subscription price. These entries may be made in journal form as follows:

(a)

Unissued Capital Stock*	$50,000.00	
Authorized Capital Stock.................		$50,000.00
An issue of 500 shares of common capital stock, par value $100 per share, authorized.		

(b)

Subscriptions Receivable..................	$50,000.00	
Capital Stock Subscribed.................		$50,000.00
Received subscriptions to capital stock as follows: J. A. Bryant, 250 shares W. L. Wood, 125 shares Richard Smith, 125 shares		

(c)

Bank..................................	$25,000.00	
Subscriptions Receivable.................		$25,000.00
Received cash on account of subscriptions to capital stock as follows: J. A. Bryant, $12,500 W. L. Wood, $6,250 Richard Smith, $6,250		

(2) Received cash from subscribers to capital stock to complete payment of balances due as follows:

J. A. Bryant..............................	$12,500.00
W. L. Wood...............................	6,250.00
Richard Smith............................	6,250.00

This transaction involves an increase in the asset cash and a decrease in the asset Subscriptions Receivable. The transaction may be recorded in journal form as follows:

Bank..................................	$25,000.00	
Subscriptions Receivable.................		$25,000.00
Received cash in payment of the balance due from subscribers to capital stock as follows: J. A. Bryant, $12,500 W. L. Wood, $6,250 Richard Smith, $6,250		

*When both common stock and preferred stock are authorized in the charter of a corporation, separate accounts should be kept for each class of stock.

(3) Issued certificates of stock to the following subscribers who had paid their subscriptions in full:

J. A. Bryant	250 shares
W. L. Wood	125 shares
Richard Smith	125 shares

Usually certificates of stock are not issued until subscriptions are paid in full. In this case the subscribers have paid their subscriptions in full and the stock certificates have been issued. The transaction may be recorded in journal form as follows:

Capital Stock Subscribed	$50,000.00	
Unissued Capital Stock		$50,000.00
Capital stock issued to subscribers as follows: J. A. Bryant, 250 shares W. L. Wood, 125 shares Richard Smith, 125 shares		

After posting all of the foregoing entries, the unissued capital stock account will be in balance and the authorized capital stock account will have a credit balance of $50,000 that represents the par value of the capital stock outstanding.

(4) J. A. Bryant returned his stock certificate for 250 shares and requested that 50 shares be transferred to W. C. Fields and that a new certificate for 200 shares be issued to himself.

This transaction indicates that Bryant has sold 50 shares of his stock to Fields. Transferring capital stock from one stockholder to another involves the cancellation of an old certificate and the issuance of new certificates for the proper number of shares. In this case, it is necessary to cancel the original certificate for 250 shares issued to Bryant and to issue two new certificates, one to Fields for 50 shares and one to Bryant for 200 shares. The transaction has no effect upon the assets, liabilities, or capital of the corporation. It is merely a transfer of stock between stockholders and the only entry required is a transfer entry in the records kept of stock issued by the corporation.

(5) The board of directors at its annual meeting held on June 15 voted to pay a cash dividend of $5 per share out of surplus, the dividend to be paid on July 1 to stockholders of record June 15.

The credit balance of the profit and loss summary account is usually transferred to the credit of the surplus account. The board of directors has the right to decide when dividends shall be paid to stockholders. After dividends have been declared, they constitute a liability of the corporation, and this liability should be recorded at the time the dividend is declared. The transaction may be recorded in journal form as follows:

June 15.	Surplus	$2,500.00	
	Dividends Payable		$2,500.00
	Dividend declared by the directors.		

Dividends may be paid immediately upon being declared or at some later date. The larger corporations usually pay dividends sometime later than the date of declaration. The directors usually specify that the dividends shall be paid to the stockholders of record as of a certain date. This means that only stockholders who have their stock recorded in their names on that date are entitled to receive dividends. Any stockholder who acquires stock after that date is not entitled to share in the dividend previously declared. To record the payment of the dividend declared in transaction No. 5, it is necessary to debit Dividends Payable and to credit the bank account as in the following journal entry:

July 1.	Dividends Payable	$2,500.00	
	Bank		$2,500.00
	Paid dividend declared June 15.		

This transaction has the effect of decreasing the liability Dividends Payable $2,500 with a similar decrease in the asset cash. After the transaction is posted, the dividends payable account will be in balance.

Incorporating a Sole Proprietorship. The legal steps involved in incorporating a sole proprietorship are the same as in organizing a new corporation. Usually the sole proprietor becomes the principal stockholder in the corporation and transfers his assets to the corporation in exchange for capital stock. His liabilities may also be assumed by the corporation. The same books of account may be continued or an entirely new set of books may be installed. Suppose, for example, that The Bryant Company, Inc. was organized to take over the business formerly conducted by J. A. Bryant as a sole proprietorship. Bryant subscribes for 200 shares of the capital stock at $100 per share and transfers his equity in the assets ($14,300) listed in his balance sheet of December 31 (reproduced on page 296) to apply on his subscription.

The entries required to record the authorized issue of capital stock and the subscriptions to the capital stock have previously been discussed and illustrated. If the books of Bryant are to be continued in use by the corporation, a simple journal entry as follows is all that is required to record the transfer of his equity to the corporation:

J. A. Bryant, Proprietor	$14,300.00	
Subscriptions Receivable		$14,300.00
Assets and liabilities of J. A. Bryant transferred to corporation at book value.		

When this entry is posted, Bryant's proprietorship account will be in balance. The following corporate accounts will take the place of Bryant's proprietorship account in the general ledger:

Authorized Capital Stock
Unissued Capital Stock
Subscriptions Receivable
Capital Stock Subscribed

If, instead of using the same books of account that were used by Bryant, a new set of books is installed by the corporation, a journal entry should be made to record the transfer of the accounts of the sole proprietorship to the corporation. If the fixed assets are being taken over at their book value, it is customary to record them in the books of the corporation at their net value after making adjustment for prior accumulated depreciation. If the fixed assets are being taken over at any value other than their book value, they should be recorded in the books of the corporation at the value agreed upon. Such value represents the cost of the assets to the corporation. The accounts of Bryant may be transferred to The Bryant Company, Inc. by means of the following general journal entry in the books of the corporation:

Bank	$4,750.00	
Accounts Receivable	3,800.00	
Merchandise Inventory	6,950.00	
Office Equipment	1,200.00	
Store Equipment	900.00	
Delivery Equipment	1,300.00	
Notes Payable		$ 1,000.00
Accounts Payable		3,200.00
Reserve for Bad Debts		400.00
Subscriptions Receivable		14,300.00
Assets and liabilities of J. A. Bryant transferred to corporation at book value.		

Assuming that Bryant paid the balance due on his subscription and that a stock certificate for 200 shares was issued to him, the transactions should be recorded in the books of the corporation as follows:

Bank	$ 5,700.00	
Subscriptions Receivable		$ 5,700.00
Cash received from J. A. Bryant in payment of balance due on subscription to capital stock.		

Capital Stock Subscribed	$20,000.00	
Unissued Capital Stock		$20,000.00
Issued 200 shares of common capital stock to J. A. Bryant.		

Incorporating a Partnership. A partnership may be terminated by incorporation and the partners may become stockholders of the corporation. The same books of account may be continued or a new set of books may be installed by the corporation. Suppose, for example, that The Bryant Company, Inc. is organized with an authorized capital of $50,000 to take over the business formerly conducted by Bryant & Wood, partners. The partners subscribe for capital stock of the corporation as follows:

J. A. Bryant, 150 shares @ $100 a share	$15,000.00
W. L. Wood, 100 shares @ 100 a share	10,000.00

Bryant and Wood, as individuals, are to receive credit toward their subscriptions for their respective equities in the assets of the partnership.

The following balance sheet for the partnership was prepared at the time of incorporating the business:

BRYANT & WOOD

BALANCE SHEET, DECEMBER 31, 19--

Assets			Liabilities	
Cash		$ 4,600.00	Notes Payable	$ 2,000.00
Notes Receivable	$ 750.00		Accounts Payable	3,738.75
Accounts Rec.	3,800.00		Total Liabilities	$ 5,738.75
	$4,550.00			
Res. for Bad Debts	300.00	4,250.00	**Proprietorship**	
			J. A. Bryant, Partner	7,246.5
Merchandise Inventory		9,800.00	W. L. Wood, Partner	7,364.7
Office Equip.	$1,600.00			
Less Res. for Depr.	500.00	1,100.00		
Delivery Equip.	$1,200.00			
Less Res. for Depr.	600.00	600.00		
Total Assets		$20,350.00	Total Liabilities and Proprietorship	$20,350.00

The authorized issue of capital stock and the subscriptions to the capital stock should be recorded as indicated in the following general journal entries:

Unissued Capital Stock	$50,000.00	
Authorized Capital Stock		$50,000.00
Authorizing the issue of 500 shares of common capital stock, par value $100 a share.		

Subscriptions Receivable	25,000.00	
Capital Stock Subscribed		25,000.00
Received subscriptions to capital stock as follows:		
J. A. Bryant, 150 shares		
W. L. Wood, 100 shares		

If the books of the partnership are to be continued in use by the corporation, the transfer of the partners' equities to the corporation may be made by means of the following general journal entry:

J. A. Bryant, Partner	$7,246.50	
W. L. Wood, Partner	7,364.75	
Subscriptions Receivable		$14,611.25
Assets and liabilities of Bryant & Wood transferred to corporation at book value.		

When this entry is posted, the partners' accounts will be in balance. If, instead of using the same books of account as were used by Bryant & Wood, a new set of books is installed by the corporation, the following journal entry in the books of the corporation is required to transfer the accounts of the partnership to the corporation:

Bank	$4,600.00	
Notes Receivable	750.00	
Accounts Receivable	3,800.00	
Merchandise Inventory	9,800.00	
Office Equipment	1,100.00	
Delivery Equipment	600.00	
Notes Payable		$ 2,000.00
Accounts Payable		3,738.75
Reserve for Bad Debts		300.00
Subscriptions Receivable		14,611.25
Assets and liabilities of Bryant & Wood transferred to corporation at book value.		

It will be noted that the fixed assets of Bryant & Wood are recorded in the books of the corporation at their net book value after making adjustments for prior accumulated depreciation. Had the fixed assets been taken over at any value other than their book value, they should be recorded in the books of the corporation at the value agreed upon.

Assuming that Bryant and Wood paid the balance due on their subscriptions and that stock certificates were issued to them, the transactions should be recorded in the books of the corporation as follows:

Bank	$10,388.75	
Subscriptions Receivable		$10,388.75
Received cash from subscribers as follows:		
W. L. Wood, $7,753.50		
J. A. Bryant, $2,635.25		

Capital Stock Subscribed	**$25,000.00**	
Unissued Capital Stock		**$25,000.00**
Issued common capital stock to subscribers.		

Corporate Accounts in the Balance Sheet. In preparing a balance sheet for a corporation the corporate accounts are usually grouped together under the heading of *capital* following the liabilities. This is known as the capital section of the balance sheet and it serves exactly the same purpose as the proprietorship section of the balance sheet for a sole proprietorship or for a partnership. At the end of the first year of operations, the capital section of the balance sheet of The Bryant Company, Inc. appeared as follows:

CAPITAL

Authorized Capital Stock	$50,000.00	
Less Unissued Capital Stock	25,000.00	
Capital Stock Outstanding		$25,000.00
Surplus		4,000.00
Total Capital		$29,000.00

It should be understood that, because of differences in capital structure, there may be considerable variation in the capital section of balance sheets prepared for different corporations. If more than one kind of capital stock is issued, each kind should be listed separately. There may be a surplus or a deficit at the end of the year. A deficit should be shown as a deduction from the par or stated value of the capital stock in arriving at the total capital of a corporation.

PRACTICE ASSIGNMENT No. 23. Complete Report No. 23 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment in Unit Twelve until Report No. 24 is required.

Unit Twelve

ACCOUNTING FOR PURCHASES

XXIV PURCHASING PROCEDURE

In many firms all incoming invoices covering credit purchases, whether they represent purchases of merchandise, supplies, or other property, are recorded in one journal. Many firms also prefer to keep the merchandise accounts on a departmental basis in order that more information may be available and better control may be exercised.

Property purchased may consist of: (a) merchandise bought for resale; (b) supplies, such as letterheads and envelopes for office use, catalogs and circulars for advertising purposes, wrapping paper and twine for use in wrapping and shipping, and cleaning supplies; or (c) fixed assets, such as office equipment, store equipment, and delivery equipment, bought for use in operating the business.

The use of a properly designed columnar journal facilitates recording all incoming invoices in one journal regardless of whether they represent purchases of merchandise, supplies, or fixed assets. It also facilitates a proper classification of essential data and makes summary posting possible.

Merchandise for resale and other property for use in the operation of a business enterprise may be purchased for cash or on credit. In one enterprise the buying may be done by the proprietor, or by an employee, and it may require only a part of his time. In another enterprise a purchasing department may be maintained with a manager in charge who may devote his entire time to buying. The successful operation of such a purchasing department requires an efficient organization and proper equipment. There should be a definite procedure for handling and recording the operations of the department.

The Purchase Requisition. Requests to purchase merchandise or other property may come to the purchasing agent or the purchasing department from any department of an enterprise. A form commonly known as a *purchase requisition* may be used for this purpose. Purchase

PURCHASE REQUISITION

BRYANT & WOOD

CHICAGO

REQUISITION No. D-129

Required for Department A

Date Issued March 27, 19—

Advise Mr. Wood on delivery

Date Required April 15, 19—

QUANTITY	DESCRIPTION
28	6.00-16 4-Ply Safety Tires
48	8.20-15 4-Ply DeLuxe Tires
24	6.50-16 4-Ply Safety Tires
40	6.00-16 Heavy Duty Tubes
60	6.70-16 Heavy Duty Tubes

Approved by J. A. Bryant

Requisition Placed by W. L. Wood

PURCHASING AGENT'S MEMORANDUM

Purchase Order No. 196

Issued to The Cole Tire Co.

Date March 27, 19—

Buffalo

Illustration No. 29, Purchase Requisition

requisitions should be numbered serially to prevent the loss or misuse of any of the forms. Usually they are prepared in triplicate, the original copy going to the purchasing agent, the duplicate copy going to the receiving clerk, and the triplicate copy being retained in the department in which the requisition originates.

A model filled-in purchase requisition form is reproduced in Illustration No. 29. The requisition specifies merchandise wanted in Department A. The mercantile business conducted by Bryant & Wood is organized into two departments. Requisitions for merchandise originate with the heads of these departments. After the purchase requisition shown in Illustration No. 29 was approved by Bryant, an order was placed with The Cole Tire Co., manufacturers of tires and tubes, as indicated by the purchasing agent's memorandum at the bottom of the form. The purchase requisition, when approved, is the purchasing department's authority to order the merchandise or other property described in the requisition.

The Purchase Order. A written order for the merchandise or other property specified in the requisition is known as a *purchase order*. A purchase order may be prepared on a printed stock form, on a specially designed form, or on an order blank supplied by the vendor. Purchase orders should be numbered serially and are usually prepared in triplicate. The original copy goes to the vendor, that is, the firm from whom the merchandise or other property is ordered; the duplicate copy is retained

PURCHASE ORDER No. 196

BRYANT & WOOD

CHICAGO

To The Cole Tire Co.
Buffalo

Date March 27, 19--
Ship Via Pa. R. R.
F. O. B. Buffalo
Terms 2/10,n/30

Deliver by Apr. 15, 19--

QUANTITY	DESCRIPTION	PRICE
28	6.00-16 4-Ply Safety Tires	11.46
48	8.20-15 4-Ply DeLuxe Tires	17.50
24	6.50-16 4-Ply Safety Tires	14.14
40	6.00-16 Heavy Duty Tubes	1.80
60	6.70-16 Heavy Duty Tubes	2.02

J. A. Bryant

Illustration No. 30, Purchase Order

by the purchasing department as its record of the order; and the triplicate copy goes to the department from which the requisition was received.

A model filled-in copy of a purchase order is reproduced in Illustration No. 30. The quantity and the description of the merchandise ordered are the same as were specified in the purchase requisition reproduced in Illustration No. 29. The unit prices shown in the purchase order are those quoted by the vendor and it is expected that the merchandise will be billed at such prices.

The Purchase Invoice. A bill rendered for property or service is commonly referred to as an *invoice.* From the viewpoint of the seller, it is considered a *sales invoice;* from the viewpoint of the buyer, it is considered a *purchase invoice.*

A purchase invoice may be received before or after delivery of the merchandise or other property ordered. As invoices are received, it is customary to number them consecutively. These numbers should not be confused with the vendor's number, which represents his sale number. After being numbered, each purchase invoice should be checked with the carbon copy of the purchase order to ascertain that the quantity, the description, the prices, and the terms agree and that the method of shipment and the date of delivery conform to the instructions and specifications. An approval form may be printed on the invoice form. Otherwise, a separate approval form may be used, or approval may be stamped on the

THE COLE TIRE COMPANY

BUFFALO

CUSTOMER'S ORDER NO. & DATE 196 March 27, 19—
REFER TO INVOICE NO. 4251
REQUISITION NO.
CONTRACT NO.
INVOICE DATE March 30, 19—
VENDOR'S NOS.

SOLD TO Bryant & Wood
542 S. Dearborn St.
Chicago, Illinois

SHIPPED TO AND DESTINATION Same

DATE SHIPPED March 31, 19— FROM Buffalo PREPAID OR COLLECT?
CAR INITIALS AND NO. F.O.B. Buffalo
HOW SHIPPED AND ROUTE Pa. R.R.
TERMS 2/10,n/30

FOR CUSTOMER'S USE ONLY

REGISTER NO. 74 VOUCHER NO.
F.O.B. CHECKED M S
TERMS APPROVED M. S PRICE APPROVED M S
CALCULATIONS CHECKED M S
TRANSPORTATION 385745 FREIGHT BILL NO. $35.29 AMOUNT
MATERIAL RECEIVED 4/10 19- DATE H. K. SIGNATURE R.C. TITLE
SATISFACTORY AND APPROVED
ADJUSTMENTS
ACCOUNTING DISTRIBUTION Acct. No. 511
AUDITED C.B. FINAL APPROVAL J.A.B.

Description		Quantity Ordered	Quantity Shipped	Excise Tax	Unit Price	Extension	Total
6.00-16	4-Ply Safety Tires	28	28	1.12	11.46	320.88	
8.20-15	4-Ply DeLuxe Tires	48	48	1.52	17.50	840.00	
6.50-16	4-Ply Safety Tires	24	24	1.24	14.14	339.36	
6.00-16	Heavy Duty Tubes	40	40	.24	1.80	72.00	
6.70-16	Heavy Duty Tubes	60	*50	.29	2.02	121.20	1,693.44
				Federal excise tax			161.08
				Total			1,854.52

*10 tubes back ordered. Will ship April 15.

Illustration No. 31, Purchase Invoice

invoice by means of a rubber stamp. If a separate approval form is used, it may be stapled to or be pasted on the invoice form.

A model filled-in purchase invoice on a standard invoice form is reproduced in Illustration No. 31. The approval form headed "For Customer's Use Only" was filled in by the purchasing department of Bryant & Wood after the invoice was received. After the invoice is approved, it should be filed with the carbon copies of the purchase order and the purchase requisition until the merchandise is received.

When the merchandise is received, the contents of the shipment may be checked with a carbon copy of the purchase order by the receiving clerk or he may prepare an independent report of the contents for the purchasing department. In the latter case the receiving clerk's report will be checked with a carbon copy of the purchase order by a clerk in the purchasing department. After the merchandise has been received and the invoice has been approved by the purchasing department, the invoice is usually referred to the accounting department where the extensions and the amounts are verified and the invoice is recorded. After the invoice is recorded by entering it in the invoice record and by posting it to the account of the creditor in the accounts payable ledger, it is usually filed in an unpaid invoice file.

Back Orders. Sometimes the vendor is unable to ship immediately a part or all of the merchandise ordered. He may, however, render an invoice immediately and indicate thereon what has been back ordered and when shipment will be made. Reference to the purchase invoice reproduced in Illustration No. 31 will show that 60 6.70–16 Heavy Duty Tubes were ordered but only 50 were shipped immediately by The Cole Tire Co. Notice of this shortage was indicated on the invoice.

Trade Discounts. Many manufacturers and wholesalers quote list prices subject to trade discounts. This makes possible the publication of catalogs with quotations of prices that will not be subject to frequent changes. Some firms, such as those dealing in hardware and jewelry, publish catalogs listing thousands of items. Such catalogs are expensive, and considerable loss might be involved where price changes occur if it were not for the fact that discount rates may be changed without changing the list or catalog prices. This practice also has the advantage of permitting retail dealers to display catalogs to their customers without revealing the cost price of the merchandise.

When an invoice is subject to a trade discount, the discount is usually shown as a deduction from the total amount of the invoice. For example, if the invoice shown in Illustration No. 31 had been subject to a trade discount of 25 per cent, the discount might be stated in the body of the invoice in the following manner:

Description	Quantity Ordered	Quantity Shipped	Excise Tax	Unit Price	Extension	Total
6.00-16 4-Ply Safety Tires	28	28	1.12	11.46	320.88	
8.20-15 4-Ply DeLuxe Tires	48	48	1.52	17.50	840.00	
6.50-16 4-Ply Safety Tires	24	24	1.24	14.14	339.36	
6.00-16 Heavy Duty Tubes	40	40	.24	1.80	72.00	
6.70-16 Heavy Duty Tubes	60	*50	.29	2.02	121.20	1,693.44
				Less 25% discount		423.36
						1,270.08
				Federal excise tax		161.08
				Total		1,431.16

*10 tubes back ordered. Will ship April 15.

In recording the invoice the amount to be entered is the net amount after deducting the discount; trade discounts should not be entered in the accounts of either the seller or the buyer, as they represent merely a reduction in the price of the merchandise.

Sometimes a series or chain of trade discounts is allowed. For example, the list prices may be subject to discounts of 25, 10, and 5 per cent. In computing the total discount where two or more trade discounts are allowed, each discount is computed separately on the successive net amounts. For example, if the gross amount of an invoice is $100 and discounts of 25, 10, and 5 per cent are allowed, the net amount should be computed as follows:

Gross amount of invoice	$100.00
Less 25%	25.00
Balance	$ 75.00
Less 10%	7.50
Balance	$ 67.50
Less 5%	3.38
Net amount	$ 64.12

In recording this invoice only the net amount, or $64.12, should be entered.

Cash Discounts. Many firms follow the practice of allowing cash discounts as an inducement for prompt payment of invoices. The terms of payment should be indicated on the invoice. It will be noted that the terms specified on the invoice reproduced in Illustration No. 31 are "2/10, n/30." This means that a discount of 2 per cent will be allowed if payment is made within 10 days from the date of the invoice, that is, if payment is made by April 9.

Should the invoice be paid on or before April 9, 2 per cent, or $33.87, may be deducted from the cost price of $1,693.44 and a check for $1,820.65 may be issued in full settlement of the invoice. After April 9 no discount will be allowed and the total amount, or $1,854.52, must be paid not later than 30 days after the date of the invoice, that is, by April 29.

Cash discounts are usually ignored at the time of recording purchase invoices, even though it may be the policy of a firm to pay all invoices in time to get the benefit of any cash discounts offered. For example, the invoice reproduced in Illustration No. 31 should be recorded by debiting the proper accounts and by crediting Accounts Payable for $1,854.52. The discount taken at time of payment on or before April 9 will be entered at the time of recording the check issued in settlement of the invoice. Thus, cash discounts are treated as income rather than as a reduction in the cost of merchandise purchased.

Sometimes an invoice is subject to both trade and cash discounts. In such case the trade discount should be deducted from the gross amount of the invoice before the cash discount is computed. For example, if the invoice reproduced in Illustration No. 31 had been subject to a trade discount of 25 per cent and the terms were 2/10, n/30, the net amount payable within 10 days from the date of the invoice should be computed in the following manner:

Amount of invoice (not including excise tax)	$1,693.44
Less trade discount, 25%	423.36
Amount subject to discount	$1,270.08
Less cash discount, 2%	25.40
	$1,244.68
Add federal excise tax	161.08
Net amount payable	$1,405.76

Usually an invoice must be paid in full within the time specified in order to obtain the benefit of any cash discount offered. However, in some instances the purchaser may be allowed the usual cash discount for partial payment of an invoice within the time specified. Thus if, instead of paying the invoice of The Cole Tire Co. in full, Bryant & Wood had made a payment of $300 on the invoice by April 9, The Cole Tire Co. might agree to allow them the cash discount of 2 per cent. In such case the amount of the discount should be computed in the following manner:

100% = amount for which Bryant & Wood should receive credit
100% − 2% = 98%
98% = $300
$300 ÷ 98% = $306.12
$306.12 − $300 = $6.12 discount

This transaction should be recorded in the books of Bryant & Wood by debiting Accounts Payable for $306.12, by crediting Purchases Discount for $6.12, and by crediting the bank account for $300.

Federal Excise Taxes. A tax on tires and inner tubes is imposed on manufacturers, producers, or importers. It is the custom of manufacturers of tires and inner tubes to list the excise tax separately on the invoice as shown in Illustration No. 31. The tax may be passed on to wholesalers, retailers, or consumers, provided the tax is stated separately on all invoices. Such taxes are in no case subject to cash discount.

Terms. The following terms are commonly used in connection with purchase invoices:

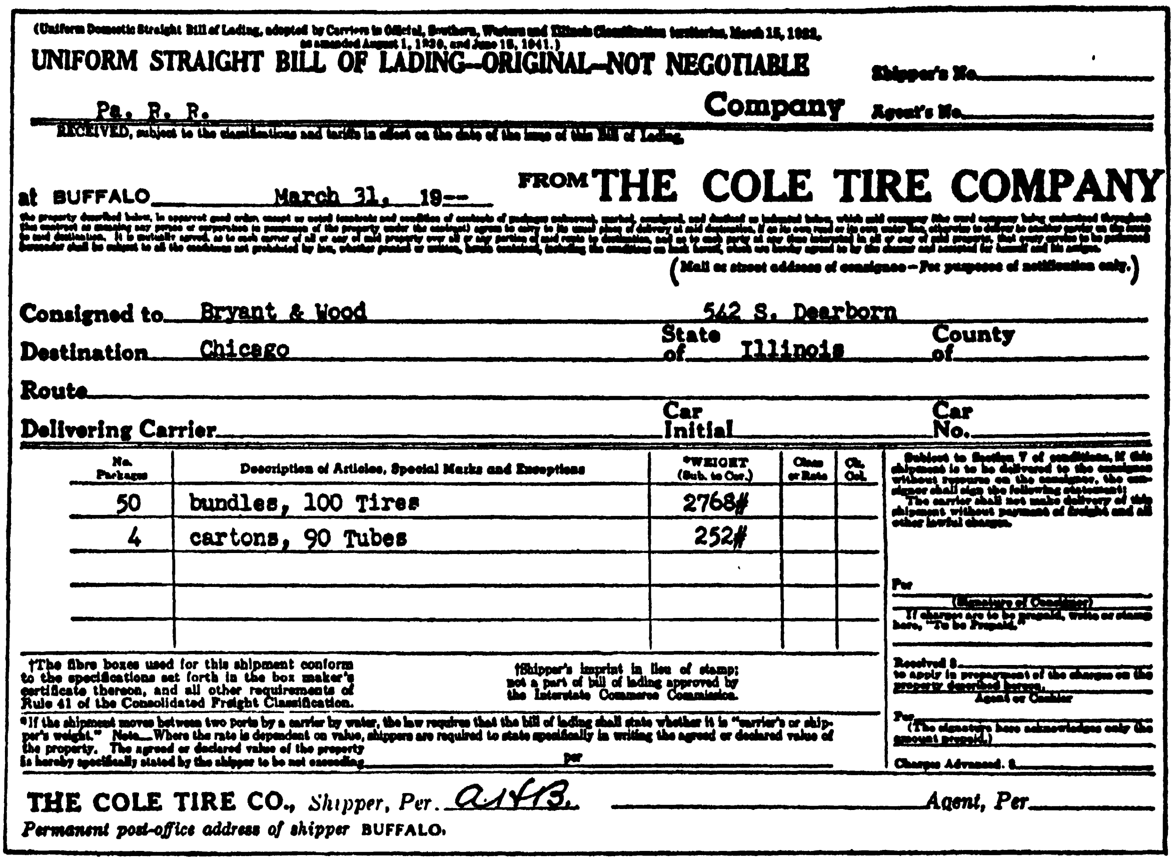
30 days	The amount of the invoice must be paid within 30 days from its date.
2/10, n/30	A discount of 2% will be allowed if payment is made within 10 days from the date of the invoice; otherwise, the total amount of the invoice must be paid within 30 days from its date.
2/E.O.M., n/60	A discount of 2% will be allowed if payment is made before the end of the month; otherwise, the total amount of the invoice must be paid within 60 days of its date.
C.O.D.	Collect on delivery. The amount of the invoice must be paid at the time the merchandise is delivered.
F.O.B. Shipping Point	Free on board at point of origin of the shipment. Under such terms the buyer must pay all transportation charges and assume all risks from the time the merchandise is accepted for shipment by the carrier.
F.O.B. Destination	Free on board at destination of the shipment. The seller will pay the transportation charges and will assume all responsibility for the merchandise until it reaches the carrier's delivery point at destination.

Miscellaneous Forms. In addition to the forms previously discussed, there are a number of miscellaneous forms such as bills of lading, freight bills, drayage bills, and credit memorandums that may be used in connection with the purchase of merchandise and other property. It is important that the function of these forms be understood in order that they may be properly handled.

Bills of Lading. The desired method of shipment is usually specified in the purchase order and the actual method of shipment is indicated in the purchase invoice. When shipment is made by freight via railroad or truck, the shipper is given a receipt that is known as a *bill of lading.*

A bill of lading is usually prepared in triplicate. The first copy is referred to as the original, the second copy as the shipping order, and the third copy as the memorandum. The freight agent signs all three copies, returning the original and the memorandum to the shipper and retaining the shipping order. The shipper in turn sends the original copy to the buyer and retains the memorandum for his files.

The merchandise or other property is delivered to the freight agent in cases, cartons, bundles, or packages; hence the description in the bill of lading may differ from the description in the purchase invoice. In addition to describing the merchandise in the bill of lading, the number of packages and the weight of each are indicated. The freight rate depends



UNIFORM STRAIGHT BILL OF LADING—ORIGINAL—NOT NEGOTIABLE

Shipper's No.

Pa. R. R. Company Agent's No.

at BUFFALO March 31, 19-- FROM THE COLE TIRE COMPANY

Consigned to Bryant & Wood 542 S. Dearborn

Destination Chicago State of Illinois County of

Route

Delivering Carrier Car Initial Car No.

No. Packages	Description of Articles, Special Marks and Exceptions	*Weight (Sub. to Cor.)	Class or Rate	Ck. Col.
50	bundles, 100 Tires	2768#		
4	cartons, 90 Tubes	252#		

THE COLE TIRE CO., Shipper, Per A.H.B. Agent, Per

Permanent post-office address of shipper BUFFALO.

Illustration No. 32, Straight Bill of Lading

upon the type of merchandise being shipped, the distance it is being shipped, and the weight of the shipment. The rate on a carload (C.L.) is lower than the rate on less than a carload (L.C.L.).

A model filled-in bill of lading is reproduced in Illustration No. 32. This is known as a *straight bill of lading,* under the terms of which title to the merchandise passed to Bryant & Wood when the merchandise was delivered to the transportation company. When Bryant & Wood present the original copy of this bill of lading to the local agent of the railroad, they will be entitled to receive the merchandise.

C.O.D. Purchases. Merchandise or other property may be purchased on C.O.D. terms. C.O.D. shipments may be made by parcel post, express, or freight. When such shipments are made by parcel post or express, the consignee must pay for the property at the time of delivery. The bill may include transportation charges and C.O.D. fees. In any event, the total amount paid represents the cost of the property purchased.

When C.O.D. shipments are made by freight, the amount to be collected by the transportation company should be entered immediately below the description of the merchandise on the bill of lading. A copy of the sales invoice should be inserted in an envelope, and the envelope should be pasted to the outside of the package, carton, or case. The transportation company will then collect the amount specified at the time of delivering the merchandise and will in turn remit to the shipper.

Make checks payable to

FREIGHT BILL

THE PENNSYLVANIA RAILROAD COMPANY CHICAGO FRONT AND BUTLER STS.

Dr., For Charges on Articles Transported:

SECTION

DATE April 2, 19--

FREIGHT BILL NO. 385745

CONSIGNEE 29 X

ROUTE (Point of Origin to Destination)

DESTINATION Bryant & Wood, Chicago, Ill.

Way-Billed From	Way-Bill Date and No.	Full Name of Shipper	Car Initials and No.
Buffalo	1829 Mar. 31	The Cole Tire Co.	C 29475
Point and Date of Shipment	Connecting Line Reference	Previous Way-Bill Reference	Original Car Initials and No.

NUMBER OF PACKAGES, ARTICLES AND MARKS	WEIGHT	RATE	FREIGHT	ADVANCES	TOTAL
50 Bundles, 100 Tires	2768#	1.53	42.35		42.35
4 Cartons, 90 Tubes	252#	1.53	3.86		3.86
TOTAL PREPAID:					
RECEIVED PAYMENT				TOTAL	46.21

FREIGHT AGENT F. B. Kline

Original paid freight bills must be surrendered for overcharges to be refunded and must accompany claims for overcharge, loss or damage.

Illustration No. 33, Freight Bill

Freight Bills. At the time merchandise or other property is delivered to a transportation company for shipment, an agent of the transportation company prepares a bill for the amount of the freight charges on the shipment. This bill is known as a *waybill.* The original copy of the waybill is forwarded to the agent of the transportation company at the station to which the merchandise is consigned. When the merchandise arrives at its point of destination, a bill for the freight charges is prepared. This bill is known as a *freight bill.* Usually the consignee is required to pay the freight bill before he can obtain the merchandise.

A model filled-in copy of a freight bill is reproduced in Illustration No. 33. A comparison of this freight bill with the bill of lading reproduced in Illustration No. 32 will show that it contains the same description of the merchandise; in addition, the rate and the amount of the freight charges are indicated.

Trucking companies usually make what is known as "store-door delivery." Freight shipments made by railroad may also be delivered to the consignee's place of business at no extra charge. In case such service is not rendered by the transportation company, it may be necessary for the consignee to employ a drayage company to transport the merchandise from the freight station to his place of business. In this case the drayage company will submit a bill for the services rendered. This is known as a *drayage bill.*

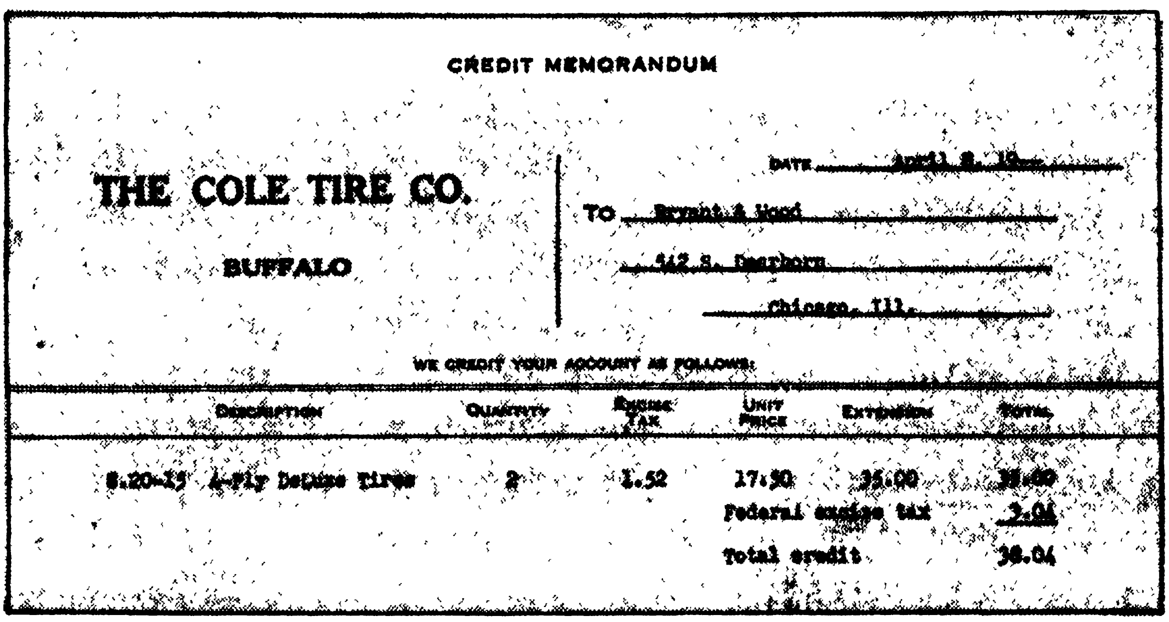
Credit Memorandums. Ordinarily the buyer expects to receive the merchandise or other property ordered and to pay for it at the agreed price in accordance with the terms specified in the purchase invoice. However, part or all of the merchandise or other property may be returned to the vendor for various reasons, such as the following:

(a) It may not conform to the specifications in the purchase order.

(b) A mistake may have been made in placing the order and the vendor may give permission for it to be returned.

(c) It may have been delayed in shipment and therefore the buyer cannot dispose of it. This sometimes happens with seasonable goods.

In some cases where the merchandise received is unsatisfactory or the prices charged are not in accord with an existing agreement or with previous quotations, an adjustment may be made that is referred to as an *allowance.*


CREDIT MEMORANDUM

THE COLE TIRE CO.
BUFFALO

DATE April 8, 19
TO Bryant & Wood
542 S. Dearborn
Chicago, Ill.

WE CREDIT YOUR ACCOUNT AS FOLLOWS:

Description	Quantity	Excise Tax	Unit Price	Extension	Total
8.20-15 4-Ply DeLuxe Tires	2	1.52	17.50	35.00	35.00
			Federal excise tax		3.04
			Total credit		38.04

Illustration No. 34, Credit Memorandum

When merchandise is returned to the supplier for credit, a charge-back invoice is usually issued for the purchase price of the merchandise returned. Upon receipt of the merchandise, the supplier will usually issue a credit memorandum for the amount of the credit allowed. A model filled-in credit memorandum is reproduced in Illustration No. 34. This form indicates that The Cole Tire Co. has given Bryant & Wood credit for the return of two 8.20–15 4-Ply DeLuxe Tires.

Standard Forms. Standard purchase order and invoice forms have been widely adopted by merchants, manufacturers, distributors, and other users. The standard invoice form was originally developed by The National Association of Purchasing Agents in collaboration with The Railway Accounting Officers Association, The National Association of

Cost Accountants, and The Association of American Railroads. The forms developed by these associations have been approved by the Division of Simplified Practice of The National Bureau of Standards, U. S. Department of Commerce. The size of the forms approved is 8½ inches wide by 7, 11, or 14 inches long. As indicated, the length may vary according to needs. As there naturally is a considerable variation in the number of items ordered at various times, an invoice form 7 inches long may be satisfactory in one case and not satisfactory in other cases. The purchase invoice shown in Illustration No. 31 was prepared on a standard invoice form.

PRACTICE ASSIGNMENT No. 24. Complete Report No. 24 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 25 is required.

XXV ACCOUNTING PROCEDURE

When all incoming invoices covering purchases on credit are recorded in one journal, regardless of whether the invoices represent the purchase of merchandise or other property, provision should be made for a proper classification of the debits and the credits. If the merchandise accounts are kept on a departmental basis, a separate column should be provided for recording the merchandise purchased for each department. The use of special columns for this purpose will facilitate summary posting. General Ledger Dr. and Cr. columns should also be provided for recording items that must be posted individually to the general ledger accounts. If individual accounts with creditors are kept in a subsidiary ledger, a summary or control account for accounts payable must be kept in the general ledger.

The procedure in recording all incoming invoices in one journal and of keeping the merchandise accounts on a departmental basis will be illustrated (a) by recording chronologically in an invoice record a narrative of selected transactions, (b) by posting direct from the purchase invoices to the individual accounts of creditors kept in a subsidiary accounts payable ledger, (c) by posting from the invoice record to the proper general ledger accounts, and (d) by preparing a schedule of accounts payable as a means of proving the accounts payable control account.

Bryant & Wood are engaged in the wholesale tire and accessories business as partners. Two departments are maintained — Dept. A, tires and tubes, and Dept. B, radios and batteries. Separate merchandise accounts are kept for each department in order that the gross operating profit for each department may be computed separately. In addition to separate departmental purchases accounts and sales accounts, separate departmental accounts are kept for transportation charges and for returns and allowances. A separate account is kept also for any federal excise taxes that are billed separately, as is the custom of manufacturers of tires and tubes. Following is a list of these accounts:

511 Sales, Dept. A
  0511 Sales Returns and Allowances, Dept. A
512 Sales, Dept. B
  0512 Sales Returns and Allowances, Dept. B
61 Purchases, Dept. A
  061 Purchases Returns and Allowances, Dept. A
62 Purchases, Dept. B
  062 Purchases Returns and Allowances, Dept. B
63 Transportation In, Dept. A
64 Transportation In, Dept. B
176 Prepaid Federal Excise Tax

Invoice Record. The form of the invoice record used by Bryant & Wood is illustrated on page 341. It should be noted that a special column is provided for recording the federal excise tax on tires and tubes. This facilitates recording the tax and makes possible summary posting of the total tax incurred each month. A narrative of the transactions that have been entered in the invoice record precedes the illustration. It will be helpful to check each transaction and to note how it was entered in the invoice record.

Corrected Purchase Invoices. If a corrected purchase invoice is received before the original invoice has been entered in the invoice record, the original invoice may be canceled and the corrected invoice may be entered in the usual manner.

If a corrected purchase invoice is received after the original invoice has been entered in the invoice record and has been posted to the individual account of the creditor, the corrected invoice may be entered either in the invoice record or in the general journal. The proper entry will depend upon whether or not the amount of the corrected invoice is more or less than the amount of the original invoice. The corrected invoice should be attached to the original invoice.

If the amount of the corrected invoice is more than the amount of the original invoice, the increase should be recorded by debiting the proper account, depending upon whether merchandise or other property was purchased, and by crediting Accounts Payable. The amount of the increase should then be posted to the credit of the proper creditor's account in the subsidiary accounts payable ledger.

If the amount of the corrected invoice is less than the amount of the original invoice, the decrease should be recorded by debiting Accounts Payable and by crediting the proper account. The amount of the decrease should then be posted to the debit of the proper creditor's account.

NARRATIVE OF TRANSACTIONS

April 1. (Saturday) Received the following purchase invoices:

No. 101, The Cole Tire Co., Buffalo; tires and tubes, $1,693.44, federal excise tax, $161.08; terms, March 30 — 2/10, n/30; freight collect.

No. 102, Pushin Auto Supply Co., Dayton; radios, $397.65; terms, March 29 — 2/10, n/30; freight collect.

No. 103, Chatfield Paper Co., City; store supplies, $56.80; terms, March 31 — 30 days.

No. 104, Modern Machine Co., City; store equipment, $75; terms, April 1 — 30-day note with interest at 6%.

5. Received a corrected purchase invoice from Pushin Auto Supply Co. for $407.65. (See purchase invoice No. 102)

25. Received the following purchase invoices:

No. 121, Hood Tire Co., Cleveland; tires and tubes, $885.75, federal excise tax, $87.60; terms, April 21 — 2/10, n/60; freight prepaid and added to invoice, $32.10.

No. 122, Western Auto Supply Co., Chicago; radios and batteries, $727.70; terms, April 22 — 1/10, n/30; freight prepaid and added to invoice, $14.

No. 123, Acme Supply Co., City; office supplies, $46; terms, April 24 — 30 days.

No. 124, The Office Equipment Co., Philadelphia; office equipment, $244; terms, April 22 — 2/10, n/30; freight prepaid and added to invoice, $17.50.

29. Received a corrected purchase invoice from the Acme Supply Co. for $40. (See purchase invoice No. 123)

Proving the Invoice Record. The invoice record may be footed and the footings may be proved at any time by comparing the sum of the debit footings with the sum of the credit footings. The footings of Bryant & Wood's invoice record were proved as of April 30 in the following manner:

Column Headings	Debits	Credits
Purchases, Dept. A	$2,579.19	
Purchases, Dept. B	1,135.35	
Federal Excise Tax	248.68	
General Ledger	491.40	
Accounts Payable		$4,373.62
General Ledger		81.00
Totals	$4,454.62	$4,454.62

INVOICE RECORD FOR MONTH OF April 19–

DEBITS: Purchases Dept A	Purchases Dept B	Federal Excise Tax	General Ledger Acct. No.	General Ledger Amount	✓	Day	Date of Inv.	Inv No.	Name	CREDITS: Accounts Payable	✓	General Ledger Acct. No.	General Ledger Amount	✓
									AMOUNTS FORWARDED					
1693.44		161.08				1	3/30	101	The Cole Tire Co.	1854.52	✓			
	397.65					1	3/29	102	Rushin Auto Supply Co.	397.65	✓			
			171	56.80	✓	1	3/31	103	Chatfield Paper Co.	56.80	✓			
			21	75.00	✓	1	4/1	104	Modern Machine Co.			35	75.00	✓
	10.00					5	3/29	102	Rushin Auto Supply Co. (corrected inv.)	10.00	✓			
885.75		87.60	63	32.10	✓	25	4/21	121	Hood Tire Co.	1005.45	✓			
	727.70		64	14.00	✓	25	4/22	122	Western Auto Supply Co.	741.70	✓			
			173	46.00	✓	25	4/24	123	Acme Supply Co.	46.00	✓			
			23	261.50	✓	25	4/22	124	The Office Equipment Co.	261.50	✓			
			36	6.00	✓	29	4/24	123	Acme Supply Co. (corrected inv.)			173	6.00	✓
2579.19	1135.35	248.68		491.40						4373.62			81.00	
(61)	(62)	(176)		(✓)						(31)			(✓)	

Ledgers. The ledgers used by Bryant & Wood include a general ledger with standard ruling and a subsidiary accounts payable ledger with balance-column ruling. The accounts affected by the transactions entered in the invoice record reproduced on page 341 are shown in skeleton form on pages 343 to 345. The March 31 balances are recorded in the accounts as of April 1. An accounts payable control account is kept in the general ledger.

Posting Procedure. Posting to Bryant & Wood's general ledger and accounts payable ledger involves both individual posting and summary posting. After each purchase invoice was entered in the invoice record, it was immediately posted to the proper creditor's account in the accounts payable ledger. The posting was done direct from the invoice, the invoice number being inserted in the Folio column.

While the posting to creditors' accounts may be done from the invoice record, there are certain advantages in posting direct from the purchase invoices. For example, the invoice provides all the information needed in posting, whereas, if the posting were done from the invoice record, it would be necessary to enter in the invoice record all the information needed in posting, regardless of whether or not it served any other purpose. Furthermore, if an error were made in entering an invoice in the invoice record, it would probably be carried over into the accounts payable ledger through the posting, whereas if the posting is done direct from the invoice, it is not likely that the same error would be made twice.

Posting direct from incoming invoices to the creditors' accounts in the accounts payable ledger is not only efficient; it also provides a sound method of internal check and control. One bookkeeper may enter the invoices in the invoice record and complete such posting as is required from the invoice record to the general ledger accounts, while another bookkeeper may post direct from the invoices to the creditors' accounts in the accounts payable ledger. Thus the work is divided between two employees, and proof of the accuracy of their work is obtained periodically by preparing a schedule of accounts payable and comparing its total with the balance of the accounts payable control account that is kept in the general ledger.

Posting to the accounts of creditors in the accounts payable ledger may be done either with a pen or with a machine. The use of posting machines for this purpose may be justifiable where there are a large number of accounts and a large number of transactions involved.

(Continued on page 346)

General Ledger

Store Supplies — Account No. 171

Date		Item	Ref.	Debit	Date		Item	Ref.	Credit
19--									
April	1	Balance	√	70.00					
	1		I341	56.80					
				126.80					

Office Supplies — Account No. 173

Date		Item	Ref.	Debit	Date		Item	Ref.	Credit
19--					19--				
April	1	Balance	√	47.50	April	29		I341	6.00
	25		I341	46.00					
		87.50		*93.50*					

Prepaid Federal Excise Tax — Account No. 176

Date		Item	Ref.	Debit	Date		Item	Ref.	Credit
19--									
April	1	Balance	√	1,454.29					
	30		I341	248.68					
				1,702.97					

Store Equipment — Account No. 21

Date		Item	Ref.	Debit	Date		Item	Ref.	Credit
19--									
April	1	Balance	√	360.00					
	1		I341	75.00					
				435.00					

Office Equipment — Account No. 23

Date		Item	Ref.	Debit	Date		Item	Ref.	Credit
19--									
April	1	Balance	√	600.00					
	25		I341	261.50					
				861.50					

Notes Payable — Account No. 35

Date	Item	Ref.	Amount	Date	Item	Ref.	Amount
				19--			
				April 1	Balance	√	400.00
				1		I841	75.00
							475.00

Accounts Payable — Account No. 36

Date	Item	Ref.	Amount	Date	Item	Ref.	Amount
19--				19--			
April 29		I841	6.00	April 1	Balance	√	1,134.75
				30		I841	4,373.62
					5,502.37		*5,508.37*

Purchases, Dept. A — Account No. 61

Date	Item	Ref.	Amount	Date	Item	Ref.	Amount
19--							
April 1	Balance	√	24,750.00				
30		I841	2,579.19				
			27,329.19				

Purchases, Dept. B — Account No. 62

Date	Item	Ref.	Amount	Date	Item	Ref.	Amount
19--							
April 1	Balance	√	18,500.00				
30		I841	1,135.35				
			19,635.35				

Transportation In, Dept. A — Account No. 63

Date	Item	Ref.	Amount	Date	Item	Ref.	Amount
19--							
April 1	Balance	√	180.00				
25		I841	32.10				
			212.10				

Transportation In, Dept. B — Account No. 64

Date	Item	Ref.	Amount	Date	Item	Ref.	Amount
19--							
April 1	Balance	√	210.00				
25		I841	14.00				
			224.00				

Accounts Payable Ledger

ACME SUPPLY CO., CITY

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Cr. Balance	√			79.50
	25	4/24—30 ds.	P123		46.00	125.50
	29	Corrected invoice	P123	6.00		119.50

CHATFIELD PAPER CO., CITY

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Cr. Balance	√			21.75
	1	3/31—30 ds.	P103		56.80	78.55

THE COLE TIRE CO., BUFFALO

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Cr. Balance	√			197.00
	1	Mdse. 3/30—2/10, n/30	P101		1,693.44	
	1	Fed. excise tax	P101		161.08	2,051.52

HOOD TIRE CO., CLEVELAND

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Cr. Balance	√			425.00
	25	Mdse. 4/21—2/10, n/60	P121		885.75	
	25	Fed. excise tax	P121		87.60	
	25	Freight prepaid	P121		32.10	1,430.45

THE OFFICE EQUIPMENT CO., PHILADELPHIA

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	25	4/22—2/10, n/30	P124		244.00	
	25	Freight prepaid	P124		17.50	261.50

PUSHIN AUTO SUPPLY CO., DAYTON

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Cr. Balance	√			84.50
	1	3/29—2/10, n/30	P102		397.65	482.15
	5	Corrected invoice	P102		10.00	492.15

WESTERN AUTO SUPPLY CO., CHICAGO

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Cr. Balance	√			327.00
	25	Mdse. 4/22—1/10, n/30	P122		727.70	
	25	Freight prepaid	P122		14.00	1,068.70

In addition to ordinary posting machines there are electric accounting machines that may be used not only as an aid in keeping accounts with creditors, but also in keeping a record of invoices and in preparing a schedule of accounts payable at the end of each accounting period. The use of mechanical devices in accounting for the operations of a business enterprise does not change the fundamental principles of double-entry bookkeeping. The primary purpose of this course is to develop these fundamentals.

Individual Posting. Each invoice entered in the Accounts Payable Cr. column of the invoice record was posted individually to the proper creditor's account in the accounts payable ledger shown on page 345. In the case of invoices involving federal excise taxes and prepaid transportation charges, the amounts of the merchandise or other property purchased, the federal excise taxes, and the transportation charges were posted separately. For example, in posting the invoice of March 30 received from The Cole Tire Co. the amount of the merchandise, $1,693.44, and the amount of the federal excise taxes, $161.08, were posted separately to the account of The Cole Tire Co.

In posting the invoice of April 22 received from the Western Auto Supply Co., the amount of the merchandise, $727.70, and the amount of the prepaid freight, $14, were posted separately to the account of the Western Auto Supply Co. The reason for posting the excise taxes and the transportation charges as separate items is that the excise taxes and the transportation charges are never subject to discount; only the amount of the merchandise purchased may be subject to discount. Since the individual posting to the accounts payable ledger was done direct from the invoices, a check mark was placed in the Check (✓) column following the Accounts Payable column of the invoice record at the time of entering the invoices.

It was also necessary to post individually each item entered in the General Ledger Dr. and Cr. columns of the invoice record. Usually this posting is completed daily. As each item was posted, a check mark was placed in the Check (✓) column following the amount column of the invoice record and the number of the invoice was entered in the Folio column of the ledger account preceding the amount posted.

Summary Posting. The summary posting is usually completed at the end of each month and involves the following procedure:

(a) The total of the column headed Purchases — Dept. A was posted to the debit of Purchases, Dept. A, Account No. 61, in the general ledger.

(b) The total of the column headed Purchases — Dept. B was posted to the debit of Purchases, Dept. B, Account No. 62, in the general ledger.

(c) The total of the column headed Federal Excise Tax was posted to the debit of Prepaid Federal Excise Tax, Account No. 176, in the general ledger.

(d) The total of the column headed Accounts Payable was posted to the credit of Accounts Payable, Account No. 36, in the general ledger.

As the total of each column was posted, the account number was written immediately below the total in the invoice record and the page of the invoice record was written in the Folio column of the general ledger as a cross reference. A check mark was placed below the totals of the General Ledger Dr. and Cr. columns in the invoice record to indicate that those totals need not be posted.

Schedule of Accounts Payable. The balance of the accounts payable control account may be proved any time after all posting is completed by preparing a schedule of the accounts with creditors from the accounts payable ledger. The following schedule was prepared from the accounts payable ledger of Bryant & Wood at the end of April and the total was checked with the balance of the accounts payable control account in the general ledger as a means of proof:

SCHEDULE OF ACCOUNTS PAYABLE

APRIL 30, 19--

Acme Supply Co.	$ 119.50
Chatfield Paper Co.	78.55
The Cole Tire Co.	2,051.52
Hood Tire Co.	1,430.45
The Office Equipment Co.	261.50
Pushin Auto Supply Co.	492.15
Western Auto Supply Co.	1,068.70
Total	$5,502.37

Cash Purchases. Bryant & Wood follow the practice of entering only credit purchases in their invoice record. Cash purchases are entered in the record of checks issued, by debiting the proper departmental purchases accounts and by crediting the bank account. Usually cash purchases are not posted to the individual accounts of creditors. However, if it is desired to post cash purchases to the individual accounts of creditors, such transactions may be entered in both the invoice record and in the record of checks issued. In other words, invoices received in connection with cash purchases may be recorded in the same manner as invoices for credit purchases, if desired.

C.O.D. Purchases. When property is purchased on C.O.D. terms, the total amount paid represents the cost of the property. Since payment must be made before possession of the property can be obtained, it is customary to treat such transactions the same as cash purchases. Thus the check issued in payment is entered in the check record by debiting the proper account and by crediting the bank account. The proper account to debit depends upon the kind of property purchased. If merchandise is purchased, the proper departmental purchases account should be debited for the cost of the merchandise and the proper departmental transportation account should be debited for the amount of any transportation charges paid. If fixed assets are purchased, the proper equipment account should be debited for the total cost, including the C.O.D. fees and any transportation charges; likewise, if supplies are purchased, the proper supply account should be debited for the total cost of the supplies, including C.O.D. fees and any transportation charges.

Transportation Charges. Express charges and freight charges may be prepaid by the shipper or may be paid by the buyer at the time of delivery. Parcel post charges must be prepaid by the shipper. Store-door delivery of freight shipments may be made by the transportation companies. However, when freight shipments are not delivered to the buyer's place of business by the transportation company, the buyer must either call for the goods at his freight station or must employ a drayman to deliver the goods to his place of business.

Transportation Charges Prepaid. If the transportation charges are prepaid by the shipper, the amount may or may not be added to the invoice, depending upon the terms of sale. If the shipper has quoted prices f.o.b. destination, it is understood that the prices quoted include transportation charges either to the buyer's place of business or to his freight station and that no additional charge will be made for any transportation charges paid by the shipper.

If the shipper has quoted prices f.o.b. point of shipment, it is understood that the prices quoted do not include the transportation charges and that the buyer will be expected to stand the transportation costs. If shipment is made prepaid, the transportation charges will be added to the invoice and the shipper will be reimbursed by the buyer when the invoice is paid.

Transportation Charges Collect. If prices are quoted f.o.b. point of shipment and shipment is made collect, the buyer must pay the transportation charges before obtaining possession of the shipment. Such transportation charges represent an addition to the cost of the merchandise or other property purchased. The method of recording the transportation charges in this case is the same as if the charges had been prepaid by the shipper and added to the invoice.

If prices are quoted f.o.b. point of destination but for some reason shipment is made collect, the buyer must pay the transportation charges before he can obtain possession of the shipment. In such cases the transportation charges paid by the buyer should be recorded as a debit to the account of the creditor from whom the merchandise or other property was ordered. In other words, the payment of the transportation charges in such case should be treated the same as a partial payment on the account of the shipper.

Transportation Accounts. As explained in Unit Two, transportation charges applicable to merchandise purchased may be recorded by debiting the purchases account. However, it is common practice to record transportation charges on incoming merchandise in a separate account, which may be entitled Transportation In or Transportation on Purchases. This account is treated as a subdivision of the purchases account and the balance must be taken into consideration in computing the cost of sales at the close of each accounting period.

The merchandise accounts of Bryant & Wood are kept on a departmental basis, with separate accounts for Purchases and for Transportation In being kept for Departments A and B. The only time transportation charges are entered in the invoice record is when they are prepaid by the shipper and are added to the invoice. For example, in recording Invoice No. 121, the prepaid freight amounting to $32.10 was charged to Transportation In, Dept. A, Account No. 63. In recording Invoice No. 122, the freight prepaid amounting to $14 was charged to Transportation In, Dept. B, Account No. 64. On all shipments by freight collect, the transportation charges will be entered in the check record. For example, when the freight charges applicable to Invoice No. 101 are paid, the amount of the check issued will be entered in the check record as a debit to Transportation In, Dept. A, Account No. 63, and as a credit to the bank account.

As a further illustration of the proper method of recording transportation charges on merchandise purchased, it will be assumed that

Bryant & Wood ordered radios and batteries from the Western Auto Supply Co. under the following variable conditions:

(a) Total amount of invoice, \$500; terms, March 1 — 1/10, n/30; f.o.b. point of shipment; freight collect, \$20.

(b) Total amount of invoice, \$520; terms, March 1 — 1/10, n/30; f.o.b. point of shipment; freight prepaid, \$20.

(c) Total amount of invoice, \$520; terms, March 1 — 1/10, n/30; f.o.b. destination; freight prepaid, \$20.

(d) Total amount of invoice, \$520; terms, March 1 — 1/10, n/30; f.o.b. destination; freight collect, \$20.

Recording transaction (a) involves an entry in the invoice record for the amount of the invoice and an entry in the check record for the amount of the check issued in payment of the freight charges. The effect of both entries is the same as in the following general journal entries:

Purchases, Dept. A	\$500.00	
Accounts Payable		\$500.00
Transportation In, Dept. A	20.00	
Bank		20.00

Recording transaction (b) involves an entry in the invoice record only. The effect of this entry is indicated by the following general journal entry:

Purchases, Dept. A	\$500.00	
Transportation In, Dept. A	20.00	
Accounts Payable		\$520.00

Recording transaction (c) involves an entry in the invoice record only. The effect of this entry is indicated by the following general journal entry:

Purchases, Dept. A	\$520.00	
Accounts Payable		\$520.00

Recording transaction (d) involves an entry in the invoice record for the amount of the invoice and an entry in the check record for the amount of the check issued in payment of the freight charges. The effect of these entries is indicated by the following general journal entries:

Purchases, Dept. A	\$520.00	
Accounts Payable		\$520.00
Accounts Payable	20.00	
Bank		20.00

It will be noted that in recording transactions (a) and (b) Purchases, Dept. A is debited for $500 and Transportation In, Dept. A is debited for $20. In recording transactions (c) and (d) Purchases, Dept. A is debited for $520. Thus the total cost of the merchandise purchased is the same in all four transactions.

Transportation charges applicable to fixed assets such as office equipment, store equipment, or delivery equipment should be treated as an addition to the cost of such equipment. For example, in entering the invoice of April 22 received from The Office Equipment Co. in the invoice record of Bryant & Wood, the total amount of the invoice, $261.50, including transportation charges amounting to $17.50, was charged to Office Equipment, Account No. 23. It is immaterial whether the freight charges are prepaid by the shipper and added to the invoice or whether shipment is made collect. If the freight is prepaid and added to the invoice, the total cost, including the invoice price and the transportation charges, may be recorded as a debit to the office equipment account in one amount. On the other hand, if shipment is made collect, the amount of the invoice should be posted in one amount and the freight charges in a separate amount as debits to the office equipment account.

Parcel Post Insurance. Merchandise or other property shipped by parcel post mail may be insured against loss or damage in transit. Such insurance may be purchased from the government through the post office, may be purchased from private insurance companies, or may be carried by the shipper at his own risk. If the cost of insurance is charged to the customer and is added to the invoice, it represents an addition to the cost of the merchandise or other property purchased. Thus, if an invoice is received for merchandise purchased and the merchandise is billed at a total cost of $100 plus postage amounting to $1 and insurance amounting to 25 cents, the total cost of the merchandise is $101.25. The purchaser may indicate in placing an order that he does not want the merchandise insured. When the purchaser indicates that he does not want merchandise insured when shipment is made by parcel post, he indicates that he is willing to assume the risk for any loss or damage sustained in transit. Title to merchandise ordinarily passes to the purchaser when it is placed in the hands of the post office for delivery.

The cost of insurance is seldom recorded separately in the books of the buyer, but is either charged direct to the purchases account or is included with transportation charges and is charged to Transportation In.

Purchases Returns and Allowances. When a credit memorandum is received as a result of merchandise returned for credit or because of an allowance made by the seller, it should be recorded by debiting Accounts Payable and by crediting the proper merchandise account. The individual account of the creditor should also be debited for the amount of the credit memorandum.

The proper merchandise account to credit for the amount of a credit memorandum received depends upon the classification of the merchandise accounts. Bryant & Wood keep separate purchases, purchases returns and allowances, and transportation accounts for Departments A and B; therefore, any credit memorandums received by them should be recorded in their books by crediting the proper departmental account for purchases returns and allowances. For example, if a credit memorandum for $175 is received from the Western Auto Supply Co. for batteries returned, it should be recorded as indicated in the following general journal entry:

Accounts Payable...............................	$175.00	
Purchases Returns and Allowances, Dept. B.....		$175.00

The credit memorandum should also be posted to the debit of the individual account of the Western Auto Supply Co. in the subsidiary accounts payable ledger.

PRACTICE ASSIGNMENT No. 25. Complete Report No. 25 in the workbook and submit your working papers to the instructor for approval. Then continue with the next study assignment in Unit Thirteen until Report No. 26 is required.

Unit Thirteen

ACCOUNTING FOR SALES

XXVI SELLING PROCEDURE

The organization of a sales department and the procedure in handling purchase orders received may vary widely depending upon many factors, such as the nature of the merchandise sold, the volume of sales, the methods of selling, the terms, etc. The purchase order must be interpreted, terms determined, credit approved, a sales invoice prepared, goods packed and shipped or delivered, and collection made before the sales transaction has been entirely completed.

Merchandise may be sold either at retail or at wholesale prices. In selling direct to the customer through retail stores, it is customary to prepare sales tickets, which constitute the original record of the sale. In the wholesale merchandising field, sales may be made by mail or through salesmen; in either case, purchase orders received constitute the basis for sales transactions. The terms on which merchandise is sold affect the procedure in handling orders and in recording the sales transactions.

Terms of Sale. The terms on which sales are made vary widely in the retail and the wholesale merchandising fields. The bases on which sales may be made are as follows:

(a) For cash.
(b) On account.
(c) C.O.D.
(d) On approval.
(e) On installment.
(f) On consignment.

Cash Sales. Some firms sell merchandise for cash only, while others sell merchandise either for cash or on credit. In department stores and certain other retail establishments the usual procedure in handling cash sales is for salesclerks to prepare sales tickets in duplicate or in triplicate; one copy is given to the customer and another copy is sent to the accounting department for recording purposes. The cash received is recorded in a cash register. At the end of each day the amount of cash received is checked with the cash register tape. It may also be checked with the total of the sales tickets.

Sales on Account. Sales on account are charge sales. Merchandise may be sold on credit at either retail or wholesale prices. In retail merchandising, charge sales tickets should be approved as to credit before the merchandise is delivered to the customer. In wholesale merchandising, each purchase order should be approved as to credit before the merchandise is billed to the customer. Both retail and wholesale merchandising enterprises usually maintain credit departments, whose principal function is to pass on all sales involving credit. The success of a firm may be influenced greatly by its credit policy. If too stringent a policy is maintained, it may have an adverse effect on sales; however, if the credit policy is too liberal, excessive losses from bad debts may be sustained.

C.O.D. Sales. Merchandise or other property may be sold on C.O.D. terms; that is, *collect on delivery*. Under such terms payment must be made at the time the goods are delivered by the seller or his agent. The agent may be an employee of the seller, a messenger, the post office, an express company, a railroad company, a trucking company, a steamship company, or any common carrier.

In wholesale merchandising, C.O.D. sales are usually recorded in the same manner as charge sales. When such sales are made to out-of-town customers, the merchandise is usually delivered by parcel post, express, or freight*. If shipment is made by parcel post or express, the post office or the express company will collect for the merchandise before giving the customer possession of it and, in turn, will remit to the seller by means of a money order. When the money order is received by the seller, it is handled in the same manner as a remittance received from any other customer in full or part payment of his account.

In retail merchandising, C.O.D. sales are usually recorded as cash sales. The C.O.D. sales tickets are segregated each day and a C.O.D. list is prepared for control purposes. The merchandise is then delivered to the customer and the sale price is collected upon delivery. When the money is turned in by the driver or other agent of the seller, he is given credit for the collection on the C.O.D. list and the sale is then recorded in the same manner as cash sales. If, for any reason, the customer refuses to accept the merchandise, it is returned to stock and the sale is canceled. It should be understood that, under this plan of handling C.O.D. sales, title to the merchandise does not pass to the customer until it is delivered and paid

*The method of making C.O.D. shipments by freight and of collecting for the merchandise before it is delivered was explained in the preceding unit under the heading of C.O.D. purchases.

for; therefore the merchandise is considered to be a part of the inventory of the seller until payment is received. Usually retail merchants who sell merchandise on C.O.D. terms make their own deliveries and collections; however, delivery may be made through the post office or any common carrier.

Sales on Approval. When sales are made on approval, the customer is given the right to return the goods within a specified time; hence the sale is not complete until it is known whether the customer will retain the goods or return them. Such sales may be handled as ordinary charge sales, and any returns may be handled like ordinary sales returns. On the other hand, sales on approval may be handled the same as ordinary cash sales. Under this plan a memorandum record of the sale is kept until such time as it is definitely known that the goods will be retained by the customer. The customer must either pay for the goods or return them by a specified date. If the sale is not recorded until payment is received, it may be treated the same as an ordinary cash sale.

Sales on approval should not be confused with *will call sales.* Will call sales may be made for cash or on credit, but in either case the customer agrees to call for the goods.

Sometimes a deposit is made by the buyer with the understanding that merchandise will be held until some future date, at which time he will call for the merchandise or at his request the merchandise will be delivered to him. Accounting for such deposits is not uniform, but the usual plan is to record the deposits in the same manner as cash sales. At the same time a charge sales ticket is prepared for the balance due, and the charge sale is recorded by debiting a special accounts receivable control account and by crediting the proper sales account. Individual accounts with such customers may be kept in a special subsidiary ledger. Some retail stores refer to this ledger as a *will call ledger.*

Instead of calling for the merchandise, the customer may request delivery on a C.O.D. basis, in which case a C.O.D. slip is made for the proper amount. When the remittance is received, it is recorded in the same manner as if the customer had called for the merchandise and paid cash.

At the end of the accounting period the total amount due from customers who have made deposits on will call sales is treated in the same manner as ordinary accounts receivable. The value of the merchandise that is being held for future delivery is not included in the inventory because it has already been recorded as sold.

Procedure in Handling Purchase Orders. In the field of wholesale merchandising, sales usually result from purchase orders received by mail, telephone, telegram, or cablegram. Purchase orders received by mail may be written on the purchase order form, letterhead, or other stationery of the buyer or on an order blank furnished by the seller. Orders received by telephone should be carefully recorded on forms provided for that purpose. The procedure in handling purchase orders varies widely with different firms; nevertheless, it is important that there be a well organized plan for handling orders. The purpose of such a plan should be to promote efficiency and to maintain an internal check that will tend to prevent mistakes in handling orders.

Interpretation. Each purchase order received should be interpreted as to (a) identity of the customer and (b) quantity and description of items ordered. Orders may be received from old or new customers. Sometimes it is difficult to identify a new customer, particularly where there has been no previous correspondence with him or where he has not been contacted by a salesman. In some cases the identity of the items ordered involves considerable difficulty because customers frequently are careless in describing the merchandise wanted. Different items of merchandise may be specified by name, stock number, or code word. Care should be used to make sure that the stock number or the code word agrees with the description of the item. Code words are commonly used in ordering by telegram or by cablegram.

Transportation. In handling each purchase order, it is necessary to determine how shipment will be made and how the transportation charges will be handled. Shipment may be made by parcel post, express, or freight. Parcel post packages may be insured. Express shipments may be made by rail or air. Freight shipments may be made by rail, air, truck, or water. The transportation charges on parcel post shipments must be prepaid. The transportation charges on express and freight shipments may be prepaid by the shipper or may be paid by the consignee upon receipt of the shipment. When transportation charges are prepaid by the shipper, they may or may not be added to the invoice, depending upon whether prices have been quoted f.o.b. point of shipment or f.o.b. point of destination.

If shipment is to be made by freight, it is also necessary to determine the routing of the shipment. The buyer may specify how he prefers to have shipment made, in which case his request usually is granted. Where the buyer does not indicate any preference, the shipper must determine whether to ship by rail, truck, air, or water, and must also frequently exercise a choice of transportation companies. Shipment to certain points may be made via different trucking companies, airlines, or railroads.

Credit Approval. All purchase orders received that involve credit in any form should be referred to the credit department or the credit manager for approval before being billed or shipped. Even C.O.D. orders should be approved by the credit department, because some customers have a reputation of not accepting C.O.D. shipments, in which case they are returned to the shipper at his expense. Customers who abuse the C.O.D. privilege may be required to send cash with the order, either in full or part payment. Some firms follow a policy of requiring part payment in cash with all orders for merchandise to be shipped C.O.D. It is a good business policy on the part of anyone to establish credit with those from whom he purchases merchandise.

Calculation. The unit prices specified on purchase invoices should be checked, the proper extensions should be made, and the total should be recorded. This operation may be performed by special clerks with the aid of calculating machines.

Billing. The next step in the handling of a purchase order is billing or preparing the sales invoice.

The purchase order reproduced in Illustration No. 35 was received by the Kruse Hardware Co. The information recorded in the spaces pro-

PURCHASE ORDER

No. 229

R. W. AURNER
328 Main Street
CLINTON

To Kruse Hardware Company
Riverside

Date May 8, 19--
Ship Via Insured Parcel Post
F. O. B.
Terms 2/10,n/30

Deliver May 15, 19--

QUANTITY	DESCRIPTION	PRICE
3	#8466 G. E. Clocks	1.50
3	#74190 G. E. Clocks	2.65
1 doz.	Lufkin Spring Joint Rules	9.20
½ doz.	#5009 Paper Holders	8.57
2 doz.	2½# Rutland Patching Plaster	2.20
20 boxes	#1 Insulated Staples (50)	.07

Received May 9, 19--
Credit O.K. J.M.
Billed May 9, 19--

C. M. Morris

Illustration No. 35, Purchase Order Received

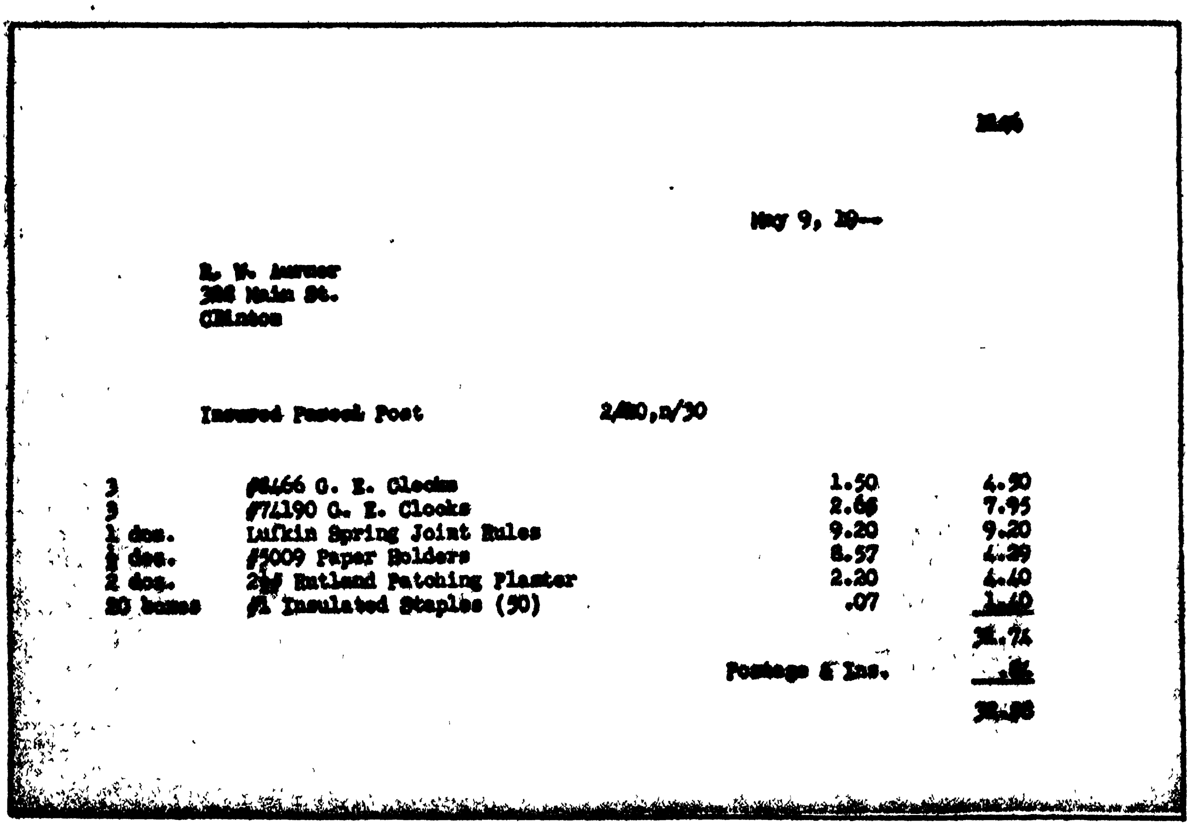
vided by the rubber stamp impression shows that the order was received on May 9, that the credit of the purchaser was approved by the credit department, and that the goods were billed on the same day the order was received. After the goods were billed, the purchase order was filed alphabetically under the name of the customer for future reference.

In the case of a wholesale merchant, the sales invoice is usually prepared on a typewriter or a billing machine. Any desired number of copies may be prepared with the aid of carbon paper. At least three copies usually are considered necessary, the original copy going to the customer as an acknowledgment of his order, the duplicate copy going to the accounting department for recording purposes, and the triplicate copy going to the shipping department as authority for packing and shipping the merchandise. The duplicate copy of the sales invoice reproduced in Illustration No. 36 is based on the purchase order received from R. W. Aurner reproduced in Illustration No. 35. Each sales invoice should be numbered consecutively.

Additional copies of the sales invoice may serve the following purposes:

(a) One copy may go to the salesman in whose territory the sale is made.

(b) One copy may go to a branch office, if the sale is made in a territory served by that office.



May 9, 19--

R. W. Aurner
Main St.
Clinton

Insured Parcel Post 2/10,n/30

3	#8466 G. E. Clocks	1.50	4.50
3	#74190 G. E. Clocks	2.65	7.95
1 doz.	Lufkin Spring Joint Rules	9.20	9.20
doz.	#5009 Paper Holders	8.57	4.29
2 doz.	Rutland Patching Plaster	2.20	4.40
20 boxes	Insulated Staples (50)	.07	1.40
			[illegible].74
		Postage & Ins.	[illegible]
			[illegible]

Illustration No. 36, Carbon Copy of Sales Invoice for Accounting Department

(c) One copy may serve as a label to be pasted on the carton or package in which shipment is made. Usually this copy is perforated so that only that part containing the name and the address of the consignee is used as the label.

Parcel Post Insurance. Merchandise shipped by parcel post mail may be insured against loss or damage in transit. Such insurance may be purchased from a post office or from a private insurance company, or the risk may be assumed by the shipper.

If parcel post insurance is purchased from the government through the post office, it is necessary only to attach the required amount of stamps to cover the additional charge for the insurance and to obtain a receipt at the time of mailing the package. A model filled-in copy of one form of receipt is reproduced in Illustration No. 37. The rate depends upon the value of the parcel. If the parcel is lost or the merchandise is damaged in transit, the government will reimburse the shipper upon receipt of claim and proof of loss.

The cost of government insurance is usually accounted for in the same manner as ordinary postage. The total value of stamps purchased is recorded by debiting Postage Stamps and by crediting the bank account. Usually a memorandum record of the stamps used on parcel post shipments is kept until the end of the month, when the total is recorded by debiting Transportation Out and by crediting Postage Stamps.

RECEIVED from Name Kruse Hardware Company
Address Riverside

the following-described pieces of Insured *mail.*
(Insert "Insured," "C. O. D.," or "Ordinary")

NOTE.—Additional receipted copies of this bill will be furnished as certificates of mailing only upon payment of one cent for each article listed on each additional copy of this bill.

	Number of Article	Name of Addressee, Street, and Post-Office Address	Postage (exclusive of other charges or fees)	Insurance or C. O. D. fee	Amount due sender if C. O. D.	†Indorsement on article	Return receipt fee	Special delivery fee	*Special handling charge	Restricted delivery fee / Remarks
1	401	R. W. Aurner, 328 Main St., Clinton	.69	.15						
2										
3										
4										
5										
6										
7										
8										
9										
10										
11										
12										
13										
14										
15										

*Special-handling charges apply only to fourth-class parcels. Special-delivery service also includes special-handling service.
†Mark "F" if "Fragile," "P" if "Perishable," "E" if "Eggs," "EH" if "Eggs for Hatching," "B" if "Butter," "FL" if "Fragile—Liquid," and "FLU" if "Fragile—Liquid—This Side Up."

Total number of pieces listed by sender One
(Write number here in words)

Total number of pieces received at post office ____

Postmaster, per ____
(Name of receiving employee)

(Affix stamps here for fee, if issued as a certificate of mailing)

(Postmark and date of receipt)

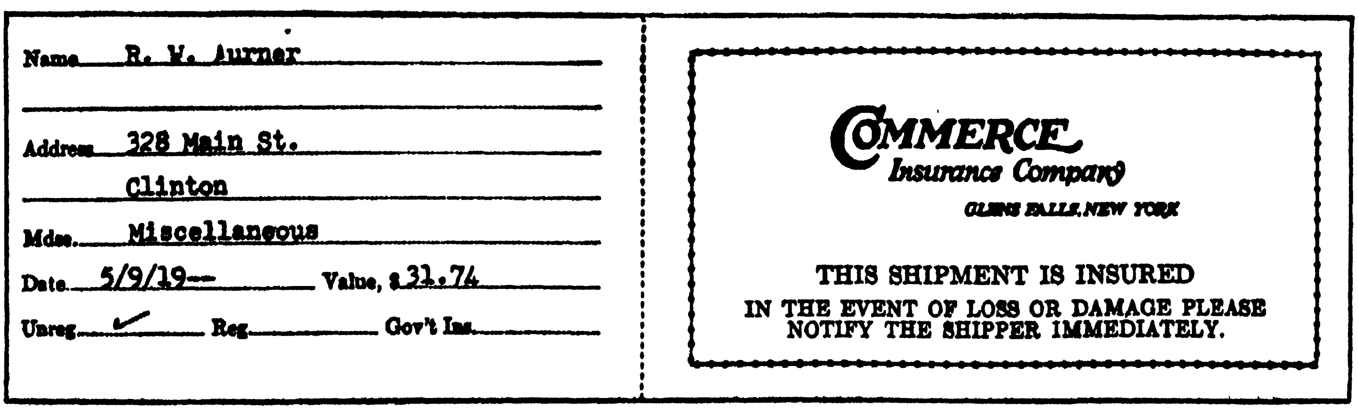
Illustration No. 37, Receipt for Insured Parcel Post Mail

When a government insured parcel post shipment is lost or damaged in transit, the amount of the loss should be ascertained and should be recorded by debiting an account with Loss on Parcel Post Shipments and by crediting Accounts Receivable in the general ledger. At the same time a credit entry should be made in the proper customer's account in the subsidiary accounts receivable ledger. A claim should then be filed with the post office for the value of the shipment. When a remittance is received from the post office in settlement of the claim, it should be recorded by debiting the bank account and by crediting Loss on Parcel Post Shipments.

When parcel post insurance is purchased from a private insurance company, a parcel post insurance coupon book is purchased. As each coupon is used, the stub is filled in as shown in Illustration No. 38. It is necessary to enclose the required number of coupons in each insured package. The number of coupons required to insure a parcel depends upon the value of the parcel and whether or not it is shipped by registered mail and/or insured parcel post. If the parcel is lost or the merchandise is damaged in transit, the insurance company will reimburse the shipper upon receipt of claim and proof of loss.

The cost of a book of coupons purchased from a private insurance company should be charged to a parcel post insurance account. The value of the coupons used in insuring each parcel is usually entered on the invoice as an additional charge to the customer and should be credited to the parcel post insurance account.

When a privately insured parcel post shipment is lost or damaged in transit, the amount of the loss should be ascertained and should be recorded by debiting an account with Loss on Parcel Post Shipments and by crediting Accounts Receivable in the general ledger. At the same time a credit entry should be made in the proper customer's account in the


Name R. V. Aurner
Address 328 Main St.
Clinton
Mdse. Miscellaneous
Date 5/9/19-- Value, $31.74
Unreg. ✓ Reg. Gov't Ins.

COMMERCE Insurance Company
GLENS FALLS, NEW YORK
THIS SHIPMENT IS INSURED
IN THE EVENT OF LOSS OR DAMAGE PLEASE NOTIFY THE SHIPPER IMMEDIATELY.

Illustration No. 38, Parcel Post Insurance Coupon with Stub

subsidiary accounts receivable ledger. A claim should then be filed with the insurance company for the value of the shipment. When a remittance is received from the insurance company in settlement of the claim, it should be recorded by debiting the bank account and by crediting Loss on Parcel Post Shipments. If the parcel post insurance account has a debit balance, it indicates that all of the coupons purchased have not been used. This balance is usually listed among the current assets on the balance sheet as prepaid parcel post insurance.

If parcel post insurance is carried by the shipper at his own risk, the premium charged the customer is usually the same as for government insurance. The amounts charged to customers for insurance are usually accumulated until the end of the month, when the total is recorded as a credit to Parcel Post Insurance. Any losses sustained on insured parcel post shipments should be recorded by debiting Parcel Post Insurance and by crediting Accounts Receivable in the general ledger and crediting the proper customers' accounts in the subsidiary accounts receivable ledger. If, at the close of the accounting period, the parcel post insurance account has a debit balance, it indicates that the losses sustained during the period have exceeded the total premiums charged to customers. If the account has a credit balance, it indicates that the value of the premiums charged to customers has exceeded the total losses sustained. While a debit balance should be treated as a loss, it does not follow that a credit balance should be treated as a gain unless it is known that no insured parcels are still in transit. It is usually considered satisfactory, however, to close the account into Profit and Loss Summary at the end of each accounting period.

Discounts. Any trade discounts allowed on sales are usually shown as a deduction from the total of the sales invoice. Such discounts should not be entered in the accounts of the seller, as they represent merely a reduction in the selling price of the merchandise.

Any cash discounts offered should be indicated in the terms. Retail merchants seldom allow cash discounts, but wholesale merchants commonly allow cash discounts as an inducement for prompt payment of sales invoices. Cash discounts should be ignored at the time of recording sales invoices, for it cannot be known at that time that the customers will pay the invoices in time to earn the discounts offered. Any cash discount that is deducted from an invoice by the customer when making payment represents an expense rather than a deduction from sales; hence it is customary to record cash discounts on sales in a separate account that is usually entitled Sales Discount.

Returns and Allowances. Merchandise may be returned by the purchaser for credit or he may ask for an allowance representing a reduction in the price of the merchandise. If credit is given for merchandise returned or as an allowance, it is customary to issue a credit memorandum for the amount involved. A model filled-in copy of a credit memorandum was reproduced in Illustration No. 34.

Installment Sales. Automobiles, pianos, electric refrigerators, electric washing machines, radios, television sets, household furniture, clothing, and many other items of merchandise are marketed extensively on the installment basis. Merchants who sell on the installment basis usually protect themselves from loss in case of default by adopting one of the following plans:

(a) Title to the property is retained by the vendor until the purchaser has completely performed his part of the transaction.

(b) Title is conveyed to the purchaser immediately, subject to a lien for the unpaid portion of the selling price.

(c) Title is conveyed to the purchaser immediately, but at the same time the purchaser executes a reconveyance in the form of a chattel mortgage to the vendor.

(d) Title is conveyed to a trustee, pending performance of the contract and subject to its provisions.

A firm may be more lenient in extending credit to customers who buy on the installment basis for the reason that title to the merchandise is retained until it is fully paid for. It is customary to require a down payment representing a part of the selling price. Some firms that sell merchandise on the installment basis mark up their prices in order to obtain a higher margin of profit. One reason for this practice is that credit is extended for a longer period of time. In selling merchandise on ordinary credit terms, it may be the custom to extend credit for no more than thirty days, whereas in selling merchandise on the installment basis, credit may be extended for as long a period as a year or more on at least a part of the purchase price.

PRACTICE ASSIGNMENT No. 26. Complete Report No. 26 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 27 is required.

XXVII ACCOUNTING PROCEDURE

When the merchandise accounts are kept on a departmental basis and all sales invoices covering charge sales are recorded in a columnar sales record, provision should be made for a proper classification of the debits and the credits. A separate column should be provided for recording the charge sales of each department so as to facilitate summary posting of the totals periodically. General Ledger Dr. and Cr. columns should also be provided for recording items that must be posted individually to the general ledger accounts. If individual accounts with customers are kept in a subsidiary ledger, a summary or control account for accounts receivable must be kept in the general ledger.

The procedure in recording all charge sales invoices in one journal and of keeping the merchandise accounts on the departmental basis will be illustrated (a) by recording a narrative of selected transactions chronologically in a sales record, (b) by posting from carbon copies of the sales invoices direct to the individual accounts of customers kept in a subsidiary accounts receivable ledger, (c) by posting from the sales record to the proper general ledger accounts, and (d) by preparing a schedule of accounts receivable as a means of proving the balance of the accounts receivable control account.

Bryant & Wood are engaged in the wholesale tire and accessories business as partners. Separate departments are maintained as follows:

Department A — Tires and tubes
Department B — Radios and batteries

Separate departmental accounts are kept for sales and for sales returns and allowances as follows:

511 Sales, Dept. A
    0511 Sales Returns and Allowances, Dept. A
512 Sales, Dept. B
    0512 Sales Returns and Allowances, Dept. B

All charge sales are made on uniform terms of 2/10, n/30. Unless otherwise specified, freight and express shipments are made on a basis of transportation charges collect. In the case of parcel post shipments, the postage is added to the invoice as an additional charge to the customer. When the invoices are entered in the sales record, the prepaid transportation charges are credited to Transportation Out, Account No. 719, in the General Ledger column. Any federal excise taxes that are billed to customers must be stated separately on the sales invoices, and the amount of the tax should be credited to Prepaid Federal Excise Tax, Account No. 176.

Sales Record. The form of the sales record used by Bryant & Wood is illustrated on page 365. A special column is provided for recording the federal excise tax on tires and tubes. This facilitates recording the tax and makes possible summary posting of the total tax billed to customers each month. Following is a narrative of selected transactions that are shown recorded in the illustration:

NARRATIVE OF TRANSACTIONS

April 1. (Saturday) Made charge sales as follows:

No. 81, Reading Garage; tires and tubes, \$78.11, federal excise tax, \$5.76; batteries \$48.10; freight collect.

No. 82, Woodlawn Motor Co.; tires and tubes, \$103.20, federal excise tax, \$6.90; radio, \$41.30; express collect.

No. 83, Lang's Auto Service; tires and tubes, \$71.05, federal excise tax, \$5.93; express collect.

No. 84, Triangle Motor Co.; radio, \$49.84; postage added to invoice, 84 cents.

No. 85, Ideal Garage; batteries, \$34.65; insured parcel post, 89 cents.

5. Sent Triangle Motor Co. a corrected invoice for Sale No. 84, amounting to \$51.58.

25. Made charge sales as follows:

No. 141, Adair Service Station; tires and tubes, \$169.90, federal excise tax, \$11.25; batteries, \$83.40; freight collect.

No. 142, Woodlawn Motor Co.; tires and tubes, \$154.81, federal excise tax, \$11.85; radio, \$82.60; freight collect.

No. 143, Ideal Garage; radio, \$50.74; less credit for radio returned, \$41.30.

29. Sent Woodlawn Motor Co. a corrected invoice for Sale No. 142; tires and tubes, \$154.81, federal excise tax, \$11.85; radio, \$44.40.

29. Sold Robinson Bros., radios, \$101.48 and received 60-day, 5% interest-bearing note. (Sale No. 144.)

Corrected Sales Invoices. If a corrected sales invoice is issued before the original invoice has been entered in the sales record, the original invoice may be canceled and the corrected invoice may be entered in the usual manner.

If a corrected sales invoice is issued after the original sales invoice has been entered in the sales record and has been posted to the individual account of the customer, the corrected invoice may be entered either in the sales record or in the general journal. The proper entry will depend upon whether or not the amount of the corrected invoice is more or less than the amount of the original invoice. A copy of the corrected invoice should be attached to the copy of the original invoice.

SALES RECORD FOR MONTH OF April 19—

DEBITS									CREDITS					
GENERAL LEDGER			ACCOUNTS RECEIVABLE	✓	DAY	NAME	SALE NO.	SALES		FEDERAL EXCISE TAX	GENERAL LEDGER		
Acct. No.	AMOUNT	✓						DEPT. A	DEPT B		Acct. No.	AMOUNT	✓
						AMOUNTS FORWARDED							
			131 97	✓	1	Reading Garage	81	78 11	48 10	5 76			
			151 40	✓	1	Woodlawn Motor Co.	82	103 70	41 30	6 90			
			76 98	✓	1	Lang's Auto Service	83	71 05		5 93			
			50 68	✓	1	Triangle Motor Co.	84		49 84		719	84	✓
			35 54	✓	1	Ideal Garage	85		34 65		719	89	✓
			90	✓	5	Triangle Motor Co.	84		90				
			264 55	✓	25	Adair Service Station	141	169 90	83 40	11 25			
			249 26	✓	25	Woodlawn Motor Co.	142	154 81	82 60	11 85			
0517	41 30	✓	9 44	✓	25	Ideal Garage	143		50 74				
517	38 20	✓			29	Woodlawn Motor Co.	142				132	38 20	✓
131	101 48	✓			29	Robinson Bros.	144		101 48				
	180 98		970 72					577 07	493 01	41 69		39 93	
	(✓)		(132)					(511)	(512)	(176)		(✓)	

If the amount of the corrected invoice is more than the amount of the original invoice, the increase should be recorded by debiting Accounts Receivable and by crediting the proper departmental sales account. The amount of the increase should also be posted to the debit of the proper customer's account in the subsidiary accounts receivable ledger.

If the amount of the corrected invoice is less than the amount of the original invoice, the decrease should be recorded by debiting the proper departmental sales account and by crediting Accounts Receivable. The amount of the decrease should also be posted to the credit of the proper customer's account in the subsidiary accounts receivable ledger.

Proving the Sales Record. The sales record may be footed and the footings may be proved at any time by comparing the sum of the debit footings with the sum of the credit footings. The footings of Bryant & Wood's sales record were proved as of April 30 in the following manner:

Column Headings	Debits	Credits
General Ledger	$ 180.98	
Accounts Receivable	970.72	
Sales, Dept. A		$ 577.07
Sales, Dept. B		493.01
Federal Excise Tax		41.69
General Ledger		39.93
Totals	$1,151.70	$1,151.70

Ledgers. The ledgers used by Bryant & Wood include a general ledger with standard ruling and a subsidiary accounts receivable ledger with balance-column ruling. The accounts affected by the transactions entered in the sales record reproduced on page 365 are shown in skeleton form on pages 369 and 370. The March 31 balances are recorded in the accounts as of April 1. An accounts receivable control account is kept in the general ledger.

Posting Procedure. The use of a general ledger and an accounts receivable ledger involves both individual posting and summary posting. After each sales invoice was entered in the sales record, it was immediately posted to the proper customer's account in the accounts receivable ledger. The posting was done direct from the invoice, the invoice number being inserted in the Folio column.

While the posting to customers' accounts might be done from the sales record, there are certain advantages in posting direct from the sales invoice. For example, the invoice provides all the information needed in posting, whereas, if the posting were done from the sales record, it would be necessary to enter in the sales record all the information needed in posting whether or not it served any other purpose. Furthermore, if an error were made in entering an invoice in the sales record, it would probably be carried over into the accounts receivable ledger through the posting, whereas, if the posting were done direct from the invoice, it is not likely that the same error would be made twice.

Posting direct from the sales invoices to the customers' accounts in the accounts receivable ledger is not only efficient; it also provides a sound method of internal check and control. One bookkeeper may enter the invoices in the sales record and may complete such posting as is required from the sales record to the general ledger accounts, while another bookkeeper may post direct from the sales invoices to the customers' accounts in the accounts receivable ledger. Thus the work is divided between two employees, and proof of the accuracy of their work is obtained periodically by preparing a schedule of accounts receivable and comparing its total with the balance of the accounts receivable control account that is kept in the general ledger.

Posting to the accounts of customers in the accounts receivable ledger may be done either with a pen or with a machine. Posting machines are widely used for this purpose and are justifiable where there are a large number of accounts and a large number of transactions involved.

In addition to ordinary posting machines there are electric accounting machines that may be used not only as an aid in keeping accounts with customers, but also in keeping a record of the sales invoices and in preparing a schedule of accounts receivable at the end of each accounting period.

Some firms use the "micro-film" method of accounting for charge sales. Under this method it is customary to keep a chronological record of charge sales in the same manner as in other methods of accounting. An individual account of the transactions with each customer is also kept until the end of the month, when it is photographed. The film is then filed as a permanent record of the business done with each customer, while the individual account becomes the customer's monthly statement.

Individual Posting. Each sales invoice entered in the Accounts Receivable Dr. column of the sales record was posted individually to the proper customer's account in the accounts receivable ledger shown on page 370. In the case of sales invoices involving federal excise taxes or prepaid transportation charges, the amount of the merchandise sold, the amount of the federal excise taxes, and the amount of the prepaid transportation charges were posted separately. For example, in posting Sales Invoice No. 81, Reading Garage was debited separately for the amount of the merchandise sold, $126.21, and for the amount of the federal excise tax, $5.76. In posting Sales Invoice No. 84, the Triangle Motor Co. was debited separately for the amount of the merchandise sold, $49.84, and for the amount of the postage, 84 cents. The reason for posting the excise tax and the transportation charges as separate items is that the excise tax and the transportation charges are never subject to discount; only the amount of the merchandise sold is subject to discount. As each invoice was posted direct to the proper account in the accounts receivable ledger, a check mark was placed in the Check (√) column following the Accounts Receivable column in the sales record.

It was also necessary to post each item entered in the General Ledger Dr. and Cr. columns of the sales record. Usually this posting is completed daily. As each item was posted, a check mark was placed in the Check (√) column following the amount column of the sales record and the page number of the sales record was entered in the Folio column of the ledger account preceding the amount posted.

Summary Posting. The summary posting is usually completed at the end of each month and involves the following procedure:

(a) The total of the column headed Accounts Receivable was posted to the debit of Accounts Receivable, Account No. 132, in the general ledger.

(b) The total of the column headed Sales, Dept. A was posted to the credit of Sales, Dept. A, Account No. 511, in the general ledger.

(c) The total of the column headed Sales, Dept. B was posted to the credit of Sales, Dept. B, Account No. 512, in the general ledger.

(d) The total of the column headed Federal Excise Tax was posted to the credit of Prepaid Federal Excise Tax, Account No. 176, in the general ledger.

It will be noted that the account with Prepaid Federal Excise Tax is debited for the excise tax on merchandise purchased and is credited for the excise tax on merchandise sold; thus the balance of the account represents the amount of the excise tax on the inventory of merchandise in stock. When all merchandise that is subject to the excise tax has been sold, the account will be in balance.

(Continued on page 371)

General Ledger

NOTES RECEIVABLE — Account No. 131

19--							
April 1	Balance	√	600.00				
29		S365	101.48				
			701.48				

ACCOUNTS RECEIVABLE — Account No. 132

19--				19--			
April 1	Balance	√	1,753.55	April 29		S365	38.20
30		S365	970.72				
	2,686.07		*2,724.27*				

PREPAID FEDERAL EXCISE TAX — Account No. 176

19--				19--			
April 1	Balance	√	1,454.29	April 30		S365	41.69
30		I341	248.68				
	1,661.28		*1,702.97*				

SALES, DEPT. A — Account No. 511

				19--			
				April 1	Balance	√	36,400.00
				30		S365	577.07
							36,977.07

SALES, DEPT. B — Account No. 512

19--				19--			
April 29		S365	38.20	April 1	Balance	√	27,100.00
				30		S365	493.01
					27,554.81		*27,593.01*

SALES RETURNS AND ALLOWANCES, DEPT. B — Account No. 0512

19--							
April 1	Balance	√	275.00				
25	Returns	S365	41.30				
			316.30				

TRANSPORTATION OUT — Account No. 719

				19--			
				April 1		S365	.84
				1		S365	.89
							1.73

Accounts Receivable Ledger

ADAIR SERVICE STATION, 209 Main St., City

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Dr. Balance	√			185.25
	25	Mdse.	S141	253.30		
	25	Fed. excise tax	S141	11.25		449.80

IDEAL GARAGE, Oakland

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Dr. Balance	√			493.79
	1	Mdse.	S85	34.65		
	1	Postage	S85	.89		529.33
	25		S143	9.44		538.77

LANG'S AUTO SERVICE, 397 High St., Paris

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Dr. Balance	√			76.70
	1	Mdse.	S83	71.05		
	1	Fed. excise tax	S83	5.93		153.68

READING GARAGE, Roselawn

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Dr. Balance	√			500.00
	1	Mdse.	S81	126.21		
	1	Fed. excise tax	S81	5.76		631.97

TRIANGLE MOTOR CO., Melbourne

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Dr. Balance	√			399.81
	1	Mdse.	S84	49.84		
	1	Postage	S84	.84		450.49
	5	Corrected invoice	S84	.90		451.39

WOODLAWN MOTOR CO., Pinewood

Date		Items	Fol.	Debits	Credits	Balance
19--						
April	1	Dr. Balance	√			98.00
	1	Mdse.	S82	144.50		
	1	Fed. excise tax	S82	6.90		249.40
	25	Mdse.	S142	237.41		
	25	Fed. excise tax	S142	11.85		498.66
	29	Corrected invoice	S142		38.20	460.46

As the total of each column was posted, the account number was written immediately below the total in the sales record and the page of the sales record was written in the Folio column of the general ledger as a cross reference. A check mark was placed below the totals of the General Dr. and Cr. columns in the sales record to indicate those totals need not be posted.

Schedule of Accounts Receivable. The balance of the accounts receivable control account may be proved any time after all posting is completed by preparing a schedule of the accounts with customers from the accounts receivable ledger. The following schedule was prepared from the ledger of Bryant & Wood at the end of April and the total was checked with the balance of the accounts receivable control account in the general ledger as a means of proof:

SCHEDULE OF ACCOUNTS RECEIVABLE

APRIL 30, 19--

Adair Service Station	$ 449.80
Ideal Garage	538.77
Lang's Auto Service	153.68
Reading Garage	631.97
Triangle Motor Co.	451.39
Woodlawn Motor Co.	460.46
Total	$2,686.07

Cash Sales. Bryant & Wood follow the practice of entering charge sales only in their sales record. Cash sales are entered in the record of cash receipts by debiting the bank account and by crediting the proper departmental sales accounts. Cash sales are not posted to the individual accounts of customers. In a wholesale business there are relatively few cash sales, as most of the business is usually done on a credit basis.

C.O.D. Sales. Bryant & Wood follow the practice of recording C.O.D. sales in the same manner as credit sales. Since they are engaged in a wholesale business, a relatively large percentage of their sales are to out-of-town customers; hence several days may elapse from the date of sale until the date payment is received. C.O.D. sales are therefore recorded in the sales record in the same manner as ordinary sales. When the remittance is received from the post office, express company, trucking company, railroad company, or other common carrier, it is entered in the record of cash receipts in the same manner as other remittances received from customers to apply on account.

Transportation Charges. In the case of parcel post shipments, the postage must, of course, be prepaid. If such packages are insured, the total amount of the postage and the insurance is added to the invoice. Bryant & Wood follow the practice of making all express and freight shipments with transportation charges collect, unless the customer requests that they be prepaid and added to the invoice. Since most shipments are made collect, it is not deemed necessary to provide a special column in the sales record for recording transportation charges prepaid; instead they are entered in the General Ledger Cr. column as a credit to Transportation Out, Account No. 719.

When the express and freight charges are prepaid, the payments are entered in the record of checks issued by debiting Transportation Out and by crediting the bank account. The amount of postage stamps used on parcel post shipments is recorded by debiting Transportation Out and by crediting Postage Stamps. Usually a memorandum record of the stamps used is kept until the end of the month, when an entry is made for the total. The transportation out account should be in balance after all posting is completed at the end of the month, provided all prepaid transportation charges were charged to customers' accounts. If, however, any shipments are made f.o.b. destination, the transportation charges represent a selling expense. In this case the transportation out account will have a debit balance, which represents the amount of the expense incurred as a result of prepaying transportation charges on shipments made f.o.b. destination.

Where numerous shipments are made by parcel post, express, and freight and the transportation charges are prepaid and charged to customers, it is advisable to provide a special credit column in the sales record for entering the transportation charges. All transportation charges on outgoing shipments that are prepaid and added to the invoices and charged to customers should be entered in this column. At the end of the month when the summary posting is completed, the total of the column should be posted to the credit of Transportation Out.

Sales Returns and Allowances. When a credit memorandum is issued to a customer for the value of merchandise returned for credit or because of an allowance made on merchandise sold, it should be recorded by debiting the proper merchandise account and by crediting Accounts Receivable. The individual account of the customer should also be credited for the amount of the credit memorandum.

The proper merchandise account to debit for the amount of a credit memorandum issued depends upon the classification of the merchandise accounts. If all sales transactions are recorded in a single sales account, that account should be debited for the amount of any credit memorandums issued that represent the value of merchandise returned by customers or the amount of any allowances made on merchandise sold.

Bryant & Wood keep separate departmental accounts for sales and for sales returns and allowances; therefore, any credit memorandums issued by them should be recorded in their books by debiting the proper departmental account for sales returns and allowances. For example, if a credit memorandum for $38.20 is issued to the Woodlawn Motor Co. for a radio returned for credit, it should be recorded as indicated in the following general journal entry:

Sales Returns and Allowances, Dept. B.............	$38.20	
Accounts Receivable..........................		$38.20
Issued credit memorandum to Woodlawn Motor Co.		

The credit memorandum should also be posted to the credit of the individual account of the Woodlawn Motor Co. in the subsidiary accounts receivable ledger.

If transactions involving the issuance of credit memorandums are numerous, a special sales returns and allowances journal may be used to advantage. Such a journal should be designed similar to the sales record reproduced on page 365, except that there should be columns provided on the debit side for recording departmental sales returns and allowances and a column provided on the credit side for recording accounts receivable. The effect of an entry to record credit allowed for merchandise returned is the reverse of an entry to record merchandise sold; therefore, if a special journal is used, its columnar arrangement should be the reverse of the columnar arrangement of the sales record.

Accounting for Installment Sales. Under the Federal Income Tax Law, dealers in personal property have the option of reporting the income from installment sales either on (a) the accrual basis or (b) the installment basis. If the accrual basis is used, the profit on installment sales is accounted for in the same manner as the profit on ordinary charge sales. If the installment basis is used, the profits are accounted for in the period in which the installments are collected rather than in the period in which the sales are made. Following is a more detailed discussion of the two methods:

(*a*) *Accrual Basis.* When installment sales are accounted for on the accrual basis, they should be recorded in the same manner as charge sales,

SALES RECORD FOR MONTH OF APRIL 19--

DEBITS										CREDITS						
General Ledger			Accounts Rec.	✓	Inst. Accts. Rec.	✓	Day	Name	Sale No.	Sales		Inst. Sales		General Ledger		
Acct. No.	Amount	✓								Dept. A	Dept. B	Dept. A	Dept. B	Acct. No.	Amount	✓
								Amounts Forwarded								
					500 00	✓	20	*C. H. Andrews*				500 00				

that is, by debiting Accounts Receivable and by crediting Sales. Usually an installment sales contract will be executed at the time of the sale and a notation of the terms will be made in the individual account of the customer in the subsidiary accounts receivable ledger. Under this plan, any anticipated loss on deferred installments should be provided for in the same manner as on ordinary charge sales, that is, through a reserve for bad debts. Since the dealer usually retains title to the merchandise until the final installment is paid, he can recover the merchandise in case of failure to make payments as agreed. Any loss sustained will be the difference between the amount charged the customer under the contract and the total amount collected in installments plus the amount realized from the resale of the repossessed merchandise. Any losses sustained should be charged to the reserve for bad debts account.

(*b*) *Installment Basis.* When installment sales are accounted for on the installment basis, a control account for installment accounts receivable should be kept in the general ledger and the individual accounts of installment customers should be kept in a subsidiary installment accounts receivable ledger. To facilitate the recording of transactions affecting installment accounts receivable, it is advisable to provide a special debit column in the sales record for installment accounts receivable and a special credit column for installment sales. If the business is departmentalized, a separate installment sales column should be provided for each department. Such a sales record is illustrated on page 374.

This form of sales record may be used in recording both installment sales and ordinary credit sales. After each installment sales invoice is recorded in the sales record, it should be posted direct to the individual account of the customer in the subsidiary installment accounts receivable ledger. Sometimes a special account form is used for this ledger. Such an account form is reproduced in Illustration No. 39.

At the end of the month when the summary posting is being completed, the total of the installment accounts receivable column of the sales record should be posted to the debit of the installment accounts receivable control account in the general ledger. The totals of the departmental sales columns should also be posted to the credit of the proper departmental sales accounts in the general ledger.

To facilitate the recording of payments received to apply on installment accounts receivable, a special column should be provided in the record of cash receipts. After each payment is recorded in this journal, it should be posted direct to the credit of the individual customer's account in the installment accounts receivable ledger. At the end of the month

COLLECTION DAY 1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31

INSTALLMENT LEDGER

TERMS $25 WEEKLY SEMI-MONTHLY MONTHLY ✓	NAME C. H. Andrews
OCCUPATION Salesman COLLECTION DAY 20th	ADDRESS 4410 St. Johns Place
KEEPS HOUSE ✓ ROOMS BOARDS HOW LONG	REMOVED
MARRIED ✓ HUS. NAME	
OWN PROPERTY WHERE	
EMPLOYED AT HOW LONG	REFERENCE The Second National Bank

CHARGES					PAYMENTS								
DATE		REMARKS	FOLIO	AMOUNT	DATE		FOLIO	AMOUNT	BALANCE	DATE	FOLIO	AMOUNT	BALANCE
19— Apr.	20	Furniture	S	500 00	19— Apr.	20	C	25 00	475 00				

Illustration No. 39, Installment Sales Account Form

when the summary posting is being completed, the total of this column should be posted to the credit of the installment accounts receivable control account in the general ledger.

At the end of the year the percentage of gross profit to be realized on the total installment sales should be determined, and this rate should be applied to the sum of the down payments and the installment payments collected during the year to find the gross profit realized on the installment sales for the year. The difference between the gross profit to be realized and the gross profit actually realized on the basis of installments collected should be treated as a deferred profit applicable to installment accounts receivable. The procedure in computing the gross profit on installment sales realized during the accounting period may be summarized as follows:

(1) Ascertain the gross profit to be realized on installment sales by deducting the cost of the merchandise sold on installment terms from the total installment sales.

(2) Ascertain the percentage of gross profit to be realized on installment sales by dividing the gross profit to be realized by the total installment sales.

(3) Apply this rate of gross profit to the sum of the down payments and the installment payments collected during the year to ascertain the amount of the gross profit actually realized.

To illustrate, assume that on April 20 a furniture dealer sold an article that cost $400 to C. H. Andrews for $500 under a sales contract calling for a down payment of $25 and monthly installments of $25 each. The effect of these transactions on the accounts of the dealer is indicated by the following general journal entries:

Purchases	$400.00	
Accounts Payable		$400.00
Purchased furniture.		
Installment Accounts Receivable	500.00	
Installment Sales		500.00
Sold furniture on installment basis.		
Bank	25.00	
Installment Accounts Receivable		25.00
Down payment. (Each monthly installment collected subsequently should be recorded in like manner.)		

The gross profit realized on the installments collected during the year may be computed in the following manner:

First Step. Ascertain gross profit to be realized.

Total installment sales	$500.00
Less cost of sales	400.00
Gross profit to be realized	$100.00

Second Step. Ascertain percentage of gross profit to be realized.

Gross profit to be realized, $100 ÷ total installment sales, $500 = 20%.

Third Step. Apply rate of gross profit to payments collected during year.

Amount of down payment collected	$ 25.00
Amount of monthly installments collected (8 × $25)	200.00
Total collections during year	$225.00
Percentage of gross profit realized	20%
Gross profit realized	$ 45.00

When the installment sales account is closed at the end of the year the gross profit realized should be credited to Profit and Loss Summary and the remainder of the gross profit to be realized should be credited to Deferred Gross Profit on Installment Sales. Following is an illustrative general journal entry:

Installment Sales	$500.00	
Cost of Sales		$400.00
Profit and Loss Summary		45.00
Deferred Gross Profit on Installment Sales		55.00
Closing the installment sales account and transferring the gross profit to the proper accounts.		

In preparing the balance sheet at the end of the year, the balance of the installment accounts receivable account amounting to $275 should be classified as a current asset, while the deferred gross profit on installment sales amounting to $55 should be listed among the liabilities as a deferred credit.

In preparing the profit and loss statement at the end of the year the gross profit realized on installment sales, amounting to $45, should be included in arriving at the total gross profit on sales. Sometimes a schedule of profits realized on installment sales is prepared to accompany the profit and loss statement. Such a schedule is illustrated at the top of the following page.

PROFITS REALIZED ON INSTALLMENT SALES

FOR PERIOD ENDED DECEMBER 31, 19--

Installment Sales	$500.00
Less Cost of Sales	400.00
Gross Profit to be Realized	$100.00
Less Deferred Gross Profit on Installment Sales	55.00
Gross Profit Realized on Installment Sales	$ 45.00

If this information is not provided in a schedule, it should be embodied in the profit and loss statement so that the information will be available to those concerned.

PRACTICE ASSIGNMENT No. 27. Complete Report No. 27 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 28 is required.

XXVIII CONSIGNMENT SALES

Produce may be shipped to commission merchants on consignment and merchandise may be shipped to dealers on consignment. Title to produce and merchandise so consigned is retained by the shipper, known as the *consignor*, until the goods are sold by the merchant or dealer, known as the *consignee*. At the time the goods are shipped to the consignee, an *invoice of shipment* is rendered. While this invoice of shipment may be similar to a sales invoice, it should be understood that a consignment shipment is not a sale. The function of the invoice of shipment is to notify the consignee of the quantity and to provide a description of the items in the shipment. Unit prices may or may not be extended on the invoice of shipment depending upon whether the produce or the merchandise is to be sold at current market prices or at prices stipulated by the consignor.

Produce, such as livestock, poultry, eggs, fresh fruits, and vegetables, is widely marketed on the consignment basis. Such shipments are usually made to commission merchants on consignment to be sold at the prevailing market prices. At the time of remitting for the produce, the consignee renders a statement of consignment sales, sometimes referred to as an *account sales*, showing the amount of the sales, the amounts of the expenses charged to the consignor, and the amount of the net proceeds. Expenses charged to the consignor may include transportation charges, storage, insurance, and other similar expenses incurred in handling the consigned goods. If the consignee is allowed a commission on sales or a discount from the selling price, the amount of his commission or discount will also be deducted in arriving at the amount of the net proceeds to be remitted to the consignor.

Incandescent lamps, radio and television tubes, electric motors, garden seeds, and many other products are also widely marketed on the consignment basis. Such goods are usually shipped to dealers or other agents on consignment to be sold at prices stipulated by the consignor. Instead of receiving a commission, the consignee may be allowed certain discounts from the consignor's list prices based upon the consignee's volume of sales.

Invoice of Shipment. A model filled-in copy of an invoice of shipment covering incandescent lamps shipped by a wholesale distributor to a retail hardware store on consignment is reproduced in Illustration No. 40. The original copy of the invoice of shipment goes to the consignee and a duplicate copy is retained by the consignor as his record of the shipment.

THE QUEEN CITY ELECTRIC CO.

AGENT OF

LAMP DEPARTMENT

UNIVERSAL ELECTRIC

COMPANY

YOUR ORDER NO.	YOUR ORDER DATE		DATE SHIPPED	INVOICE DATE	INVOICE NO.
	6/6/19—	TERMS AS PER YOUR CONTRACT	6/7/19—	6/7/19—	GL 7939

CHARGE TO

OAKWOOD HARDWARE CO.
OAK ST.
CITY

SHIPPED TO OAKWOOD HARDWARE CO.

QUANTITY	SPECIFICATION ABBREVIATIONS OR WATTS-VOLT-BULB-BASE-FINISH	UNIT LIST PRICE	AMOUNT	TOTAL
	CHARGE YOUR LAMP CONSIGNMENT ACCOUNT			
48	25 A	.13	6.24	
48	60 A	.14	6.72	
24	75 A	.16	3.84	
24	100 A	.16	3.84	
24	10 S11/W	.21	5.04	25.68

CONSIGNMENT OF ELECTRIC LAMPS TO BE HELD BY THE AGENT, AND TO BE SOLD OR DISTRIBUTED ONLY IN ACCORDANCE WITH THE EXISTING CONTRACT WITH THE AGENT.

Illustration No. 40, Invoice of Shipment

Note that the invoice of shipment provides the dealer with detailed information relative to the merchandise that has been charged to his account, including specifications of the items, the quantities, the unit list prices, the extended amount of each item, and the total amount of the shipment.

The duplicate copy of the invoice of shipment provides the information needed in recording merchandise shipped on consignment. The invoice may be recorded in the general journal, or a special consignment shipments record may be kept if desired. Accounts with consignees may be kept in the general ledger, or, if preferred, a subsidiary consignment ledger may be kept with a control account in the general ledger.

Statement of Consignment Sales. Periodically, usually at the end of each month, the consignor mails the consignee a partially completed statement of merchandise consigned to him. This statement shows (a) the value of the consigned merchandise in the consignee's hands at the beginning of the month, (b) a summary of the consignment shipments made during the month and (c) the total amount of consigned merchandise for which the consignee must account. On the basis of an inventory taken at the end of the month, the consignee completes the statement by calculating (a) the volume of the sales he has made of consigned merchandise during the month, (b) his compensation, and (c) the amount of the proceeds he should remit to the consignor.

A model filled-in statement of consignment sales is reproduced in Illustration No. 41. In the statement reproduced, the balance forwarded from the previous month's statement, amounting to $348.92, represents the amount charged to the consignee at the beginning of June. The items listed in the body of the statement indicate the value of the merchandise shipped to the consignee during June. The amount listed on line 1 of the agent's monthly report, $447.46, is the sum of the items listed in the body of the statement. This includes the balance forwarded from the previous statement plus the sum of the shipments during the month. The basic compensation indicated in the statement is based on a contract agreement between the consignor and the consignee.

Accounting for Consignment Sales. As previously explained, produce and merchandise may be consigned to a commission merchant or a dealer to be sold at the prevailing market prices or at stipulated prices. Because of varying conditions, methods of accounting for consignment sales are not uniform. Produce or merchandise that is shipped on consignment to be sold at prevailing market prices may be charged to the consignee at wholesale prices or no charge at all may be made. In the latter case a memorandum record of the shipment will be kept by the consignor. Merchandise that is shipped on consignment to be sold at stipulated prices may be billed to the consignee either at wholesale prices or at retail prices. The principal effect of such shipments is to transfer the goods from one place to another, with the consignor retaining title to the goods. It is, of course, advisable to keep some record of the consignments in order that the location and the value of the goods may be determined at any time. The value of the goods out on consignment must be included in the consignor's

STATEMENT OF **MERCHANDISE** CONSIGNED BY

LAMP DEPARTMENT

UNIVERSAL ELECTRIC

COMPANY

TO AGENT . Oakwood Hardware Co.
Oak St.
City

THRU SERVING AGENT . The Queen City Electric Co.

FOR MONTH ENDED	FORM AND BASIS	APPOINTMENT EXPIRES	TOTAL LIST SALES TO & INCLUDING LAST REPORT	TOTAL LIST SALES TO QUALIFY NEXT BASIS
6/30/19--	A-300	9/1/19--	840.99	

DATE OR OTHER REFERENCE	DEBIT	CREDIT	BALANCE
BALANCE FORWARDED FROM PREVIOUS STATEMENT			348.92
6/7 Gl 7939	25.68		
6/19 Gl 7579	28.80		
6/21 Gl 7795	18.24		
6/27 Gl 8311	16.22		
6/30 Gl 7691	9.60		

RETURN 2 SIGNED COPIES TO YOUR SERVING AGENT

AGENT'S MONTHLY REPORT

1	CONSIGNMENT BALANCE AS PER STATEMENT ABOVE	447.46
2	LIST VALUE OF CONSIGNED STOCK ON HAND AT END OF MONTH★	327.39
3	LIST VALUE OF SALES REPORTED THIS MONTH (LINE 1 LESS 2)	120.07
4	BASIC COMPENSATION (30 % OF LINE 3)	36.02
5	LIST VALUE OF SALES LESS BASIC COMPENSATION (LINE 3 LESS 4)	84.05
6	SPECIAL COMPENSATION (5% OF LINE 5) DO NOT DEDUCT UNLESS REPORT AND PAYMENT IN FULL ARE MAILED ON OR BEFORE 7th OF MONTH	4.20
7	NET VALUE OF SALES REPORTED (LINE 5 LESS 6)	79.85
8	LIST VALUE OF NON-TAXABLE LAMPS INCLUDED IN LINE 3	
9	FEDERAL EXCISE TAX (10.1 %) OF TAXABLE LIST SALES (LINE 3 LESS LINE 8)	12.13
10	OTHER CHARGES OR CREDITS	
11	AMOUNT OF REMITTANCE TO BE MAILED TO SERVING AGENT (LINE 7 + 9 + OR — 10)	91.98

★ "If your agency appointment requires an itemized inventory at the end of each month, the amount appearing on line 2 shall be the list value of your inventory and the inventory must be recorded on the form supplied by your serving agent. If your appointment provides for reporting sales on a 'working stock' basis, the amount appearing on line 2 shall be the list value of your working stock unless you elect to take an itemized inventory, in which case the inventory must accompany this report and the list value of your inventory inserted on line 2 above."

THIS CERTIFIES THAT THE ABOVE IS A TRUE AND ACCURATE MONTHLY REPORT OF SALES AND STATMENT OF LAMPS HELD IN CONSIGNED STOCK FOR THE ACCOUNT OF THE GENERAL ELECTRIC COMPANY ON THE ABOVE DATE.

DATE July 5, 19-- SIGNED Oakwood Hardware Co. AGENT

PER T. D. Tain

AGENT PLEASE NOTE: TO EARN YOUR 5% SPECIAL COMPENSATION YOU MUST FORWARD YOUR REMITTANCE IN FULL WITH THIS REPORT ON OR BEFORE 7TH OF THE MONTH TO YOUR SERVING AGENT.

Illustration No. 41, Statement of Consignment Sales

inventory, although it is customary to list the inventory of consigned goods separately in the balance sheet, using the same method of valuation as is used in inventorying ordinary merchandise in stock.

When a statement of consignment sales is received from a commission merchant, the sales should be recorded on the books of the consignor. The proper entries will vary depending upon the method of accounting for consignment shipments. Usually a separate account will be kept for consignment sales so that such sales may be recorded separately from ordinary sales. If it is desired to record consignment sales in the sales record along with ordinary charge sales, it may be advisable to provide a special credit column to facilitate the summary posting of the total consignment sales at the end of each month. If it is customary for the consignee to remit the proceeds at the time of rendering a statement of consignment sales, the entire transaction may be entered in the record of cash receipts in much the same manner as ordinary cash sales. It may, however, be advisable to provide a special credit column in the cash receipts record so as to facilitate summary posting of the total consignment sales at the end of each month.

To illustrate, it will be assumed that a statement of consignment sales has been received from a commission merchant covering the sale of a shipment of poultry. The consignor made no entry on his books for the shipment; he simply kept a copy of the invoice of shipment as a memorandum record. This statement shows that the total sales amounted to $1,200 and that the following expenses were incurred by the consignee and charged to the consignor:

Transportation charges	$145.00
Commission	120.00

A remittance for the proceeds amounting to $935 accompanied the statement. The effect of this transaction on the accounts of the consignor is indicated by the following general journal entry:

Transportation Out	$145.00	
Commission	120.00	
Bank	935.00	
Consignment Sales		$1,200.00

Since a remittance for the amount of the proceeds was received with the statement, the transaction may be recorded completely in the record of cash receipts.

When merchandise is shipped on consignment to a dealer under contract to be sold at prices stipulated by the consignor, an entirely different accounting procedure may be advisable.

Consignor's Books. In Illustration No. 40 there is reproduced an invoice of shipment of lamps to the Oakwood Hardware Co. by The Queen City Electric Co. This invoice was recorded in the books of The Queen City Electric Co. as indicated by the following general journal entry:

Oakwood Hardware Co., Consignee	$25.68	
Consignment Shipments		$25.68
Invoice of shipment No. 7939.		

The Queen City Electric Co. follows the practice of charging the consigned merchandise to the consignee and crediting Consignment Shipments at list or retail prices. A separate account may be kept in the general ledger for each consignee, or these accounts may be kept in a subsidiary ledger with a control account in the general ledger. An account is also kept in the general ledger for consignment shipments. The accounts with the consignees are not ordinary accounts receivable because the consignees are not obligated to pay for the merchandise unless it is sold. The Queen City Electric Co., therefore, follows the practice of treating the accounts with the consignees and with consignment shipments as memorandum or offsetting accounts that are never shown in the balance sheet. On the other hand, some firms follow the practice of treating the consignees' accounts as an asset and the account with consignment shipments as deferred income to be shown as offsetting or contra items in the balance sheet.

In Illustration No. 41 there is reproduced a statement of consignment sales received from the Oakwood Hardware Co. It shows that in addition to the shipment of June 7, which amounted to $25.68, four other shipments from The Queen City Electric Co., were received during the month. When this statement was received by The Queen City Electric Co., the following entries were made to record the merchandise sold on consignment by the Oakwood Hardware Co. and the remittance received in payment of the proceeds:

Consignment Shipments	$120.07	
Consignment Sales		$120.07
Consigned merchandise sold by Oakwood Hardware Co. during June.		
Bank	$ 91.98	
Commission on Consignment Sales	36.02	
Discount Allowed on Consignment Sales	4.20	
Federal Excise Tax		$ 12.13
Oakwood Hardware Co., Consignee		120.07
Statement of consignment sales received from Oakwood Hardware Co. with remittance of $91.98 in payment of proceeds.		

The first entry was made to record the June sales of merchandise consigned to the Oakwood Hardware Co. The second entry was made to record the remittance received from the Oakwood Hardware Co. in payment of the proceeds for June sales of consigned merchandise.

The amount credited to Federal Excise Tax is the amount of the tax collected by the consignee and remitted to the consignor. The Queen City Electric Co. follows the practice of debiting Federal Excise Tax for the amount of the tax billed separately on invoices received from the manufacturer and crediting Federal Excise Tax for the amount of tax collected by the consignee.

Assuming that the Oakwood Hardware Co. was the only consignee to whom merchandise was shipped on consignment, the consignment accounts would appear in the general ledger of The Queen City Electric Co. as follows after the June transactions were posted:

OAKWOOD HARDWARE CO., CONSIGNEE

19--				19--			
June 1	Balance		348.92	June 30			120.07
7			25.68				
19			28.80				
21			18.24				
27			16.22				
30			9.60				
		327.39	*447.46*				

CONSIGNMENT SHIPMENTS

19--				19--			
June 30			120.07	June 1	Balance		348.92
				7			25.68
				19			28.80
				21			18.24
				27			16.22
				30			9.60
						327.39	*447.46*

It should be noted that the debit balance of the account with the Oakwood Hardware Co., Consignee is the same as the credit balance of the account with Consignment Shipments. This balance represents the June 30 inventory of merchandise consigned to the Oakwood Hardware Co.

Consignee's Books. At the time of receiving the invoice of shipment reproduced in Illustration No. 40, the Oakwood Hardware Co. recorded the transaction in its books as indicated by the following general journal entry:

Consigned Merchandise	$25.68	
The Queen City Electric Co., Consignor		$25.68
Invoice of shipment No. 7939.		

Other invoices of shipment received from the same consignor during the month were recorded in like manner. The account with The Queen City Electric Co. is not an ordinary account payable as there is no obligation to pay for the consigned merchandise unless it is sold. The Oakwood Hardware Co. follows the practice of treating the accounts with consignors and with consigned merchandise as memorandum or offsetting accounts that need not appear in the balance sheet.

As the consigned merchandise was sold by the Oakwood Hardware Co., the sales were recorded by debiting the bank account or Accounts Receivable, depending upon whether the sales were for cash or on account, and by crediting Sales for the selling price and crediting Federal Excise Tax for the amount of the tax added to the selling price of the merchandise. At the end of the month an inventory of the consigned merchandise was taken and the statement of consignment sales, reproduced in Illustration No. 41, was completed by filling in the agent's monthly report at the bottom of the form. This statement, together with a remittance for $91.98, was then mailed to The Queen City Electric Co. prior to July 7 in order to get the benefit of the special 5 per cent compensation allowed. This transaction was recorded in the books of the Oakwood Hardware Co. as indicated by the following general journal entries:

Sales	$120.07	
Consigned Merchandise		$120.07
Consigned merchandise sold during June.		
The Queen City Electric Co.	$120.07	
Federal Excise Tax	12.13	
Discount Received on Consignment Sales		$ 4.20
Commission on Consignment Sales		36.02
Bank		91.98
Statement of consignment sales rendered to The Queen City Electric Co. with remittance of $91.98 in payment of proceeds.		

The first entry was made to record the June sales of merchandise consigned by The Queen City Electric Co. After this entry was posted, the balance of the sales account represented the amount of the regular sales of other merchandise during the month. The second entry was made to record the check issued in payment of the proceeds for June sales of consigned merchandise.

Assuming that The Queen City Electric Co. is the only company from which merchandise is received on consignment, the consignment accounts would appear in the general ledger of the Oakwood Hardware Co. as follows after the June transactions were posted:

THE QUEEN CITY ELECTRIC CO., CONSIGNOR

19--			19--		
June 30		120.07	June 1	Balance	348.92
			7		25.68
			19		28.80
			21		18.24
			27		16.22
			30		9.60
				327.39	*447.46*

CONSIGNED MERCHANDISE

19--			19--		
June 1	Balance	348.92	June 30		120.07
7		25.68			
19		28.80			
21		18.24			
27		16.22			
30		9.60			
	327.39	*447.46*			

It should be noted that the debit balance of the account with Consigned Merchandise is the same as the credit balance of the account with The Queen City Electric Co., Consignor. This balance represents the June 30 inventory of merchandise consigned by The Queen City Electric Co.

The federal excise tax imposed on electric light bulbs is a manufacturer's tax that is passed on to the ultimate consumer. The tax was recorded in the books of the Oakwood Hardware Co. as a credit to Federal Excise Tax at the time of recording sales of electric light bulbs. When the June statement of consignment sales was rendered to The Queen City Electric Co., the federal excise tax collected, amounting to $12.13, was included in the remittance and was recorded as a debit to Federal Excise Tax. Thus the account with Federal Excise Tax in the books of the Oakwood Hardware Co. was in balance after recording the tax included in the June settlement.

***PRACTICE ASSIGNMENT No. 28.** Complete Report No. 28 in the workbook and submit your working papers to the instructor for approval. Then continue with the next study assignment in Unit Fourteen until Report No. 29 is required.*

Unit Fourteen

ACCOUNTING FOR NEGOTIABLE INSTRUMENTS

XXIX NEGOTIABLE NOTES

"An unconditional, written promise or order to pay a sum certain in money to a designated person or to his order, or to bearer, on demand or at a fixed or determinable future time"* is a *negotiable instrument.* The essential elements of negotiability are as follows:

(a) The instrument must be in writing and it must be signed by the party executing it.
(b) It must contain an unconditional promise or order to pay a sum certain in money.
(c) It must be payable to a designated person, or to his order, or to bearer.
(d) It must be payable either on demand or at a fixed or determinable future time.

The most commonly used negotiable instruments may be divided into three classes as follows:

(a) Checks.
(b) Notes.
(c) Drafts and trade acceptances.

Ordinary bank checks are negotiable instruments. Certified checks and cashier's checks are also negotiable instruments. A certified check is an ordinary check that has been certified by the bank on which it is drawn. Either the drawer or the payee of a check may have it certified. When a bank certifies a check, the amount is charged to the depositor's account immediately and the money is held in a special account until the check is presented for payment. The method of accounting for a certified check is the same as for an ordinary check so far as the drawer is concerned.

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*Uniform Negotiable Instruments Act.

A cashier's check is a draft drawn by the cashier of a bank on its own funds. Anyone may purchase a cashier's check. If an ordinary bank check is issued in payment of a cashier's check, the method of accounting for the check issued is identical with the method of accounting for a check issued for any other purpose.

Money orders and travelers' checks are similar to ordinary bank checks in that they constitute a written order for payment of a sum certain in money on demand. Postal money orders may be purchased from any post office; they constitute an order for the payment of a specified amount of money by any post office on demand. Express money orders may be purchased from any office of the American Express Company; they constitute an order for the payment of a specified amount of money by any office of the American Express Company. Travelers' checks may be purchased from banks, American Express Company offices, and the offices of certain other transportation companies.

Negotiable notes may be received and issued in the ordinary course of business. Notes received are commonly referred to as notes receivable, while notes issued are commonly referred to as notes payable. Notes may or may not be interest bearing. Interest is the amount charged for the use of money. It is similar to rent charged for the use of property. In some cases the interest is payable in advance, that is, it must be prepaid. Usually, however, the interest is payable at maturity of the note, or periodically until the note matures and is paid.

Calculating Interest. In calculating interest on notes, it is necessary to take the following factors into consideration:

(a) The principal.
(b) The time.
(c) The rate of interest.

The principal is the face amount or principal sum specified in a note. It is the base on which the interest is calculated.

The period elapsing from the date of a note to the date of maturity, or to the interest payment date, is the time for which the interest is computed. Thus, if a note is payable in 60 days with interest, the interest should be computed for the 60-day period. On the other hand, if a note is dated March 1 and is due May 1, the period for which the interest should be computed is 61 days.

When the time in a note is specified by months, the interest should be calculated on a basis of months rather than days. For example, if a note is payable 3 months from date, the interest should be calculated on a basis of 3 months or ¼ of a year. However, when the due date is specified in a note, the time should be computed by ascertaining the exact number of days elapsing from the date of the note to the date of maturity and the interest should be computed on the basis of such number of days. For example, if a note is dated April 1 and the due date is specified as July 1, the time should be computed in the following manner:

Days in April	30
Date of note, April	1
Days remaining in April	29
Days in May	31
Days in June	30
Note matures on July	1
Total time in days	91

In this computation it will be noted that the date of maturity was counted but the date of the note was not counted. If the due date had been specified as "3 months after date" instead of July 1, the interest should be computed on a basis of 90 days, instead of 91 days.

In the case of long-term notes, the interest may be payable periodically, such as semiannually or annually.

The rate of interest is usually expressed in the form of a percentage, such as 4 per cent or 6 per cent. Ordinarily the rate is an annual percentage rate, but in some cases the rate is quoted on a monthly basis, such as 1 per cent a month. A rate of 1 per cent a month is equivalent to a rate of 12 per cent a year payable monthly. When a note is interest bearing but the rate is not specified, it is subject to the legal rate, which varies under the laws of different states.

In computing interest it is customary to consider 360 days a year. Most banks and business firms follow this practice. However, the Federal Reserve System uses 365 days as a year in computing interest on notes rediscounted by member banks. Following is an illustration of the difference in computing interest under the two methods:

FACTORS

(a) Principal of note	$500
(b) Time	60 days
(c) Rate of interest	6%

COMPUTATIONS

360-day year	*365-day year*
6% of $500 = $30	6% of $500 = $30
60/360 of $ 30 = $5	60/365 of $ 30 = $4.93

It will be noted that under both methods the time for which the interest is being computed is used as the numerator while the number of days in the year is used as the denominator. The following formula may be applied in computing interest regardless of whether it is being computed on the basis of a 360-day year or a 365-day year:

PRINCIPAL $\times$ RATE $\times$ TIME (IN YEARS) = AMOUNT OF INTEREST

The 60-Day, 6 Per Cent Method. There are many short cuts that may be used in computing interest on the basis of a 360-day year. The interest on any amount for 60 days at 6 per cent can be ascertained by simply moving the decimal point in the amount two places to the left. The reason for this is that 60 days is $\frac{1}{6}$ of a year and the interest on any amount at 6 per cent for $\frac{1}{6}$ of a year is the same as the interest at 1 per cent for a year. Thus, the interest on $241.30 for 60 days at 6 per cent is $2.41.

The 60-day, 6 per cent method may be used advantageously in many cases even though the actual time may be more or less than 60 days. The following examples will serve to illustrate this fact:

(a)

FACTORS

(a) Principal of note, $1,000
(b) Time, 30 days
(c) Rate of interest, 6%

CALCULATION

When the decimal point is moved two places to the left the result is $10

30 days = $\frac{1}{2}$ of 60 days, hence the interest amounts to $\frac{1}{2}$ of $10 or $5

(b)

FACTORS

(a) Principal of note, $1,000
(b) Time, 120 days
(c) Rate of interest, 6%

CALCULATION

When the decimal point is moved two places to the left the result is $10

120 days = 2 times 60 days, hence the interest amounts to 2 times $10 or $20

The 60-day, 6 per cent method may also be used advantageously when the actual rate is more or less than 6 per cent. The following examples will serve to illustrate this fact:

(a)

FACTORS

(a) Principal of note, $1,000
(b) Time, 30 days
(c) Rate of interest, 3%

CALCULATION

Interest at 6% for 60 days = $10
Interest at 6% for 30 days = $5
Interest at 3% = $\frac{1}{2}$ of $5 or $2.50

(b)

FACTORS

(a) Principal of note, $1,000
(b) Time, 120 days
(c) Rate of interest, 8%

CALCULATION

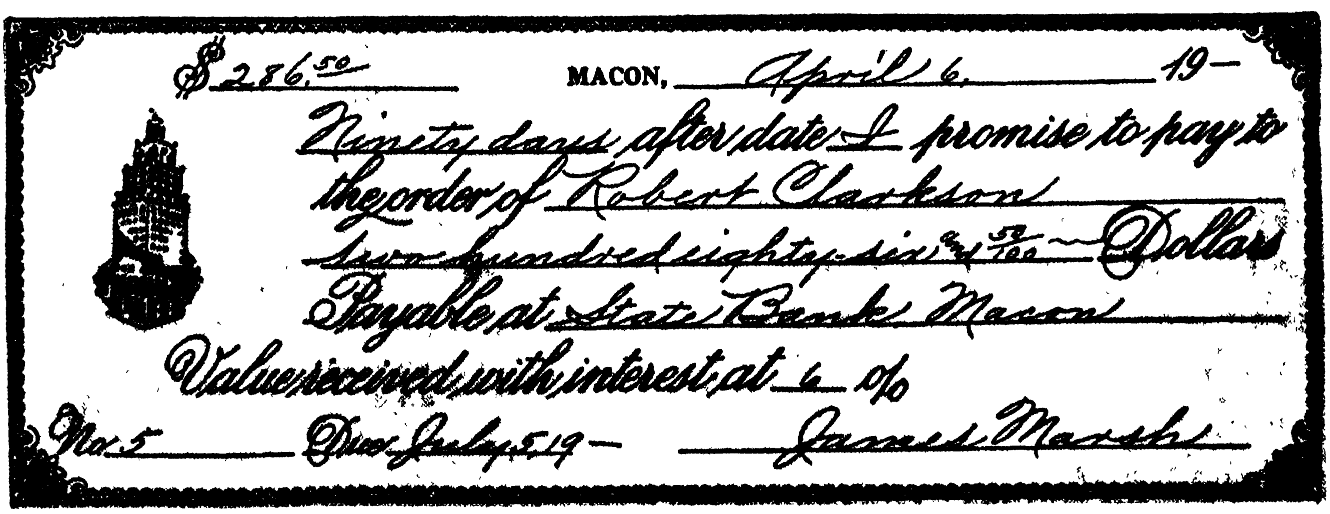
Interest at 6% for 60 days = $10
Interest at 6% for 120 days = $20
Interest at 8% = $1\frac{1}{3}$ times $20 or $26.67

Sometimes it is advantageous to ascertain the interest for 6 days at 6 per cent and to use the result as a basis for calculating the actual interest. The interest on any sum for 6 days at 6 per cent may be ascertained by simply moving the decimal point three places to the left; thus, the interest on $1,000 at 6 per cent for 6 days is $1. If the actual time were 18 days instead of 6 days, the interest would be three times $1, or $3. This method differs from the 60-day, 6 per cent method only in that 6 days is used in the basic computation instead of 60 days. In other words, the interest is first calculated for 6 days at 6 per cent and then the result is used as the basis for calculating the interest for the actual time and at the actual rate specified in the note.

Published tables are available for reference use in ascertaining the amount of interest on stated sums at different rates for any length of time. Such tables are widely used by financial institutions and may also be used by other firms. The fact that published tables are available for reference use does not lessen the importance of being able to compute interest accurately and speedily.

Present Value. The present value or *present worth* of a note is its value on any day between the date of the instrument and the maturity of the instrument. If a note is interest bearing, the present value may be ascertained by adding the accrued interest to the face of the note. If a note is noninterest bearing, the present value may be ascertained by subtracting from its face, interest at the discount rate for the time elapsing from the date as of which the present value is computed to the date of maturity.

It may be necessary to ascertain the present value of a note (a) when it is being transferred for credit or (b) when it is being sold for cash. The following note is reproduced in order that it may be used to illustrate the method of calculating the present value of a note:


$286.50 MACON, April 6 19—
Ninety days after date I promise to pay to the order of Robert Clarkson
Two hundred eighty-six 50/100 Dollars
Payable at State Bank Macon
Value received with interest at 6 %
No. 5 Due July 5 19— James Marsh

The following alternate transactions involving the foregoing note indicate the reason for ascertaining its present value:

(a) May 16, Robert Clarkson transferred the note to Bryant & Wood, who agreed to allow him credit for its present value.

(b) May 16, Robert Clarkson sold the note to the Liberty National Bank at a discount of 7 per cent.

In transaction (a) the note is transferred for credit at its present value. The factors involved in computing its present value are as follows:

FACTORS

(a) Principal of note, \$286.50
(b) Time interest has accrued, 40 days (April 6 to May 16)
(c) Rate of interest, 6%

CALCULATIONS

Interest accrued on \$286.50 at 6% for 40 days = \$1.91
\$286.50 + \$1.91 = \$288.41, present value

In transaction (b) the note was sold to the Liberty National Bank at a discount of 7 per cent. Such a transaction is often referred to as *discounting a note.* It is the custom of banks to calculate the discount on the maturity value of a note. The amount of the discount is then subtracted from the maturity value to find the present value of the note.

FACTORS

(a) Principal of note, \$286.50
(b) Time from date of note to date of maturity, 90 days (April 6 to July 5)
(c) Rate of interest, 6%
(d) Time from date of discount to date of maturity, 50 days (May 16 to July 5)
(e) Rate of discount, 7%

CALCULATIONS

Interest on \$286.50 at 6% for 90 days = \$4.30
\$286.50 + \$4.30 = \$290.80, maturity value
Discount on \$290.80 at 7% for 50 days = \$2.83
\$290.80 − \$2.83 = \$287.97, present value

The interest is computed on the face of the note, while the discount is computed on the maturity value of the note. Bank discount should not be confused with either trade discount or cash discount. As has been previously explained, trade discount is a discount from the list price of merchandise, while cash discount is a discount allowed for payment of an invoice within a specified time. Bank discount is interest collected in advance on a loan. Discounting a note receivable at the bank is a method of borrowing money and using the note as security. Since the party discounting the note must endorse it, he is liable for its maturity value in case the maker does not pay it at maturity.

Accounting for Notes Receivable. The following types of transactions involve notes receivable:

(a) Notes received in exchange for merchandise or other property.
(b) Notes received from customers in order to obtain an extension of time on their accounts.
(c) Notes received as security for cash loans.
(d) Notes transferred prior to maturity.
(e) Notes discounted prior to maturity.
(f) Notes paid at maturity.
(g) Notes renewed at maturity.
(h) Notes dishonored.

Notes Received in Exchange for Merchandise or Other Property. A note may be accepted in exchange for merchandise or other property. For example, Bryant & Wood accepted a 60-day, 5 per cent interest-bearing note for $101.48 in exchange for radios sold Robinson Bros. on April 29. This transaction was recorded in the sales record of Bryant & Wood by debiting Notes Receivable, Account No. 131, and by crediting Sales, Dept. B, for $101.48. See page 365.

Notes Received from Customers to Obtain an Extension of Time on Accounts. When a customer wishes to obtain an extension of time on his account, he may be willing to issue a note for all or part of the amount due. A merchant may be willing to accept a note from a customer who desires an extension of time on his account for the reason that it is a written acknowledgment of a debt and, if cash is needed before the note matures, it may be possible to discount it at a bank.

R. E. Brand owes Bryant & Wood $422.36 on open account. The account is past due and Bryant & Wood insist upon a settlement. Mr. Brand offers to give them his 60-day, 6 per cent interest-bearing note. Bryant & Wood accept the note, dated April 10. It was recorded in their books as indicated by the following general journal entry:

April 10.	Notes Receivable	$422.36	
	Accounts Receivable		$422.36
	Received note from R. E. Brand.		

If, instead of tendering a note for the full amount, Mr. Brand tendered a check for $22.36 and a note for the balance and Bryant & Wood accepted the check and the note, the transaction should be recorded in their books as indicated by the following general journal entry:

April 10.	Bank	$ 22.36	
	Notes Receivable	400.00	
	Accounts Receivable		$422.36
	Received check and note from R. E. Brand.		

Notes Received from Employees. Loans to employees may be evidenced by notes receivable. For example, Bryant & Wood might loan Robert Jackson, an employee, $100 on his 90-day, 4 per cent interest-bearing note. Such a transaction should be recorded in their books as indicated by the following general journal entry:

April 1.	Notes Receivable	$100.00	
	Bank		$100.00
	Loaned Robert Jackson $100.		

Notes Transferred Prior to Maturity. In order to obtain an extension of time on his account, a customer may tender a note that he has accepted from another party. For example, R. E. Brand might have tendered to Bryant & Wood a note that he had accepted from James B. Roberts and agreed to pay the balance of his account in cash. Bryant & Wood might have agreed to accept the note for credit at its present value. Assume, for example, that the face of the note amounted to $350, that it is dated March 1, and that it is due in 90 days with interest at 6 per cent. If Bryant & Wood accept this note on April 15, its present value may be computed as follows:

March 1 to April 15 = 45 days
$350 at 6% for 45 days = $2.63, interest accrued
$350 + $2.63 = $352.63, present value of note

The amount to be paid in cash is the difference between the amount of Mr. Brand's account, $422.36, and the present value of the note, $352.63, or $69.73. The transaction should be recorded in the books of Bryant & Wood as indicated by the following general journal entry:

April 15.	Bank	$ 69.73	
	Notes Receivable	350.00	
	Accrued Interest Receivable*	2.63	
	Accounts Receivable		$422.36
	Received note for $350 and check for $69.73 from R. E. Brand.		

Notes Discounted Prior to Maturity. As previously explained, a note may be discounted at a bank prior to maturity. It sometimes happens that a merchant is in need of funds to be used as working capital and, in order to obtain the necessary funds, he may discount at a bank one or

*The accrued interest on notes receivable transferred may be charged to Interest Income instead of Accrued Interest Receivable, if desired. If the accrued interest is charged to Interest Income, that account will show the proper income when it is credited for the full amount of the interest collected at the maturity of the note.

more notes that he owns. Suppose, for example, that on May 1 Bryant & Wood discounted at the Liberty National Bank the note received from Robinson Bros. on April 29 and received credit for the proceeds, the rate of discount being 6 per cent. The proceeds may be computed as follows:

Face value of note	$101.48
Interest at 5% for 60 days	.85
Maturity value of note	$102.33

Discount period May 1 to June 28 = 58 days

$102.33 at 6% for 58 days = 99¢

$102.33 − 99¢ = $101.34, proceeds

Since the note had been accepted originally by Bryant & Wood at its face value of $101.48 and the proceeds from discounting the note amounted to only $101.34, the difference of 14 cents represents interest expense. This transaction should be recorded in the books of Bryant & Wood as indicated by the following general journal entry:

May 1.	Bank	$101.34	
	Interest Expense	.14	
	Notes Receivable		$101.48
	Discounted Robinson Bros.' note at the bank.		

If the interest on the note had amounted to more than the bank discount, the difference would represent a gain which should be credited to Interest Income.

Contingent Liability on Notes Discounted. In discounting Robinson Bros.' note at the bank it was necessary for Bryant & Wood to endorse the note. This endorsement had the effect of guaranteeing payment of the note at maturity, because Bryant & Wood would have to pay it if Robinson Bros. should fail to pay it. This liability is known as a *contingent liability* for the reason that Bryant & Wood's liability is contingent upon the failure of Robinson Bros. to pay the note at maturity.

In preparing a balance sheet, it is customary to ascertain the sum of any notes that have been discounted but have not been paid by the makers and to indicate that the sum represents a contingent liability. This is usually indicated by means of a footnote to the balance sheet. The usual plan is to place an asterisk (*) after the amount of the asset, Notes Receivable, and to state the amount of the contingent liability in a footnote. For example, if the notes receivable amounted to $12,000 and notes discounted but not yet paid amounted to $2,000, the following statement should be added to the balance sheet in a footnote:

**Contingent liability on notes discounted, $2,000.*

In order to ascertain whether any notes discounted have not been paid, it may be necessary to inquire at the bank at which they were discounted. It is the custom of banks, however, to notify endorsers in case any notes discounted are not paid promptly at maturity.

Sometimes a separate account is kept with Notes Receivable Discounted. In this case notes receivable that are discounted are credited to the notes receivable discounted account instead of being credited to the notes receivable account. A record is kept of the due date of notes discounted and when it is ascertained that a note has been paid by the maker, an entry is made debiting Notes Receivable Discounted and crediting Notes Receivable. When a separate account with notes receivable discounted is kept, the balance of the account should be shown as a deduction from notes receivable on the asset side of the balance sheet, although it is sometimes listed among the liabilities under the heading of Contingent Liabilities.

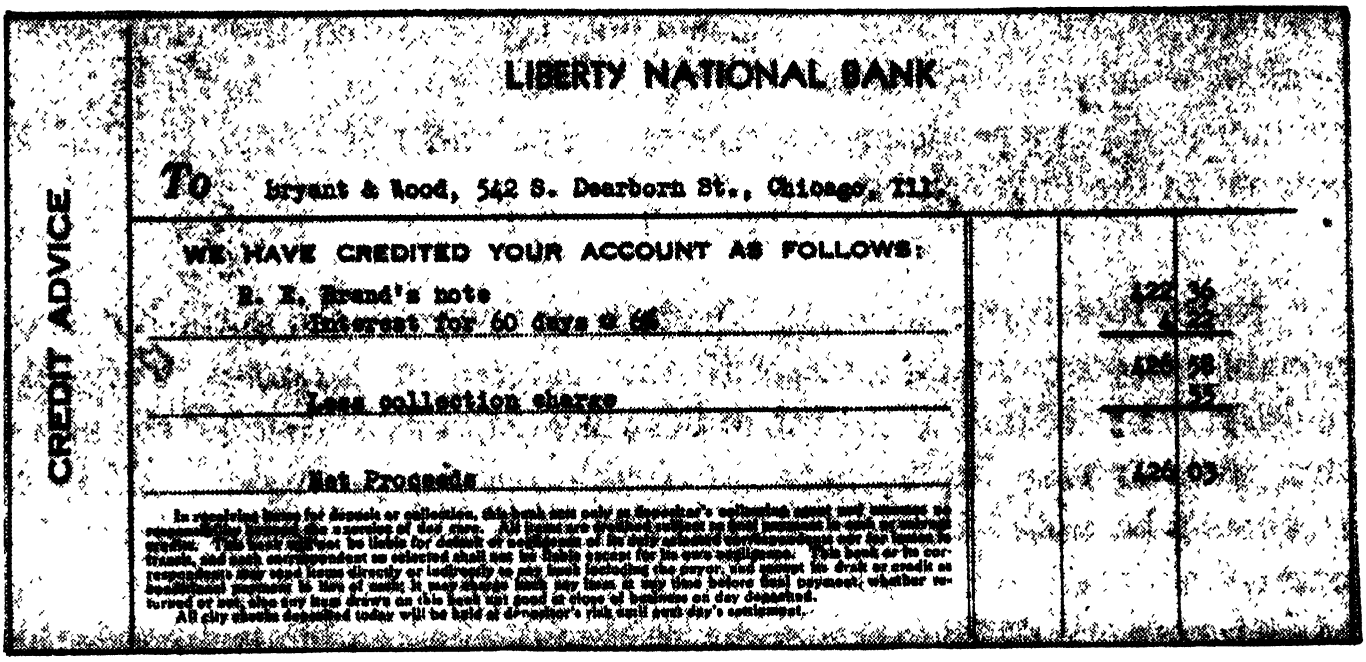
Notes Paid at Maturity. When notes receivable mature, they may be collected by the payee or he may leave them at his bank for collection. If the maker of a note resides in another locality, the note may be forwarded to a bank in his locality for collection. It is customary for banks to charge a fee for making such collections.

Usually the maker is notified a few days before the maturity of a note in order that he may know the due date and the amount payable. From the foregoing discussion it will be seen that the payment may be received direct from the maker or from a bank with whom the note has been left for collection. If Robert Jackson pays his note in full plus the interest when it matures, Bryant & Wood should record the transaction in their books as indicated by the following general journal entry:

June 30.	Bank	$101.00	
	Notes Receivable		$100.00
	Interest Income		1.00
	Received $101 from Robert Jackson in payment of his note for $100 and interest $1.		

If Bryant & Wood left R. E. Brand's note for $422.36 at the Liberty National Bank for collection and on June 10 received the notice of collection reproduced below, the transaction should be recorded in their books as indicated by the following general journal entry:

June 10.	Bank	$426.03	
	Collection Expense	.55	
	Notes Receivable		$422.36
	Interest Income		4.22
	Received credit for the proceeds of R. E. Brand's note collected by the bank.		



Notes Renewed at Maturity. If the maker of a note is unable to pay the amount due at maturity, he may be permitted to renew the note in whole or in part. If, instead of paying his note for $100 at maturity, Robert Jackson were permitted to pay the interest and renew the note for another 90 days at the same rate of interest, the transaction should be recorded in the books of Bryant & Wood as indicated by the following general journal entry:

June 30.	Notes Receivable (new note)	$100.00	
	Bank	1.00	
	Notes Receivable (old note)		$100.00
	Interest Income		1.00
	Received a new note for $100 from Robert Jackson in renewal of his note due today and $1 in cash in payment of the interest on the old note.		

Notes Receivable Register. When many notes are received in the usual course of business, it may be advisable to keep an auxiliary record of such notes that will provide more detailed information than can be provided in a ledger account. Such an auxiliary record is usually known as a notes receivable register. One form of a notes receivable register is reproduced below. The notes recorded in the illustration were those received by Wilson & Jones during the period indicated by the record.

The information recorded in the register is obtained directly from the notes received. The notes are numbered consecutively as they are entered in the register. This number should not be confused with the maker's number. The due date of each note is calculated and entered in the proper When Due column. The interest to maturity is calculated and entered in the Interest Amount column. When a note is discounted, the name of the bank at which it is discounted and the date are entered in the Discounted columns. When a remittance is received in payment of a note, the date is entered in the Paid column.

Notes Receivable Account. The information recorded in the notes receivable account should agree with that entered in the notes receivable register. The account at the top of page 399 contains a record of the notes that were entered in the notes receivable register of Wilson & Jones. It should be noted that the identity of each note is indicated by the number assigned to the note. If the notes are not numbered, the identity of each note should be indicated by writing the name of the maker in the Items column of the account.

NOTES RECEIVABLE REGISTER

Date Received		No.	By Whom Payable	Where Payable		Date Made		
				Bank or Firm	Address	Mo.	Day	Year
Mar.	28	1	W. O. Booker	City Bank	Troy	Mar.	28	19–
	30	2	C. M. Martin	First National Bank	Detroit	Mar.	30	19–
	30	3	A. W. Whitten	Union Bank	Dexter	Mar.	30	19–
Apr.	1	4	J. A. Robbins	State National Bank	Erie	Apr.	1	19–
May	15	5	R. E. Branch	City National Bank	City	May	15	19–
	18	6	James Marriner	State Bank	Mason	Apr.	6	19–
	18	7	Williams & Allison	City National Bank	City	May	18	19–
	25	8	Jason & Cox	Union Bank	Clinton	Apr.	28	19–
	29	9	A. W. Whitten	" "	Dexter	May	29	19–

(Left-hand page)

NOTES RECEIVABLE

19--				19--		
Mar. 28	No. 1		180.00	May 27	No. 1	180.00
30	No. 2		200.00	29	No. 4	492.50
30	No. 3		250.00	29	No. 2	200.00
Apr. 1	No. 4		492.50	29	No. 3	250.00
May 15	No. 5		350.00	29	No. 7	300.00
18	No. 6		286.50			*1,422.50*
18	No. 7		300.00			
25	No. 8		218.60			
29	No. 9		200.00			
		1,055.10	*2,477.60*			

Proving the Notes Receivable Account. Periodically, usually at the end of each month, the notes receivable account should be proved by comparing the balance of the account with the total of the notes owned as shown by the notes receivable register. Following is a schedule of the notes owned on May 31:

SCHEDULE OF NOTES OWNED

No. 5	$ 350.00
No. 6	286.50
No. 8	218.60
No. 9	200.00
Total	$1,055.10

It will be noted that the total of this schedule is the same as the balance of the notes receivable account reproduced above.

NOTES RECEIVABLE REGISTER

TIME	WHEN DUE J	F	M	A	M	J	J	A	S	O	N	D	AMOUNT	INTEREST RATE	INTEREST AMOUNT	DISCOUNTED BANK	DISCOUNTED DATE	PAID	REMARKS
60 ds					27								180 00	6%	1 80			May 27	
60 ds					29								200 00	—				May 29	Sent for Coll. 5/22
60 ds					29								250 00	6%	2 50			May 29	Renewal for $200
90 ds						30							492 50	6%	7 39	Liberty Nat'l	May 29		
60 ds							14						350 00	6%	3 50				
90 ds							5						286 50	6%	4 30				
60 ds							17						300 00	—		Liberty Nat'l	May 29		
60 ds						27							218 60	—					
60 ds							28						200 00	6%	2 00				Renewal of No. 3

(Right-hand page)

Endorsement of Notes. The term *endorsement,* as applied to a note, designates the writing on the back of the note for any one of the following purposes:

(a) Security.
(b) Transfer of title.
(c) Receipt for part payment.

The signature only of an individual or firm on the back of a note is known as a *blank endorsement* and indicates a pledge of security. In other words, the individual or firm endorsing the note guarantees its payment.

When the payee of a note desires to transfer title to the note to another party, he may endorse the note "Pay to the order of" and sign his name. This is known as an *endorsement in full.* Such an endorsement does not relieve the endorser from liability in case the maker fails to pay the note when it matures.

When a partial payment is made on a note, it is common practice to endorse the payment on the back of the note by writing the date and the amount paid. A signature to such an endorsement is not required. It is merely an endorsement that serves as a memorandum record of payments.

The three types of endorsements previously discussed are shown in Illustration No. 42. The first endorsement indicates security; the second endorsement indicates that the title to the note has been transferred to R. L. Foley by M. A. Allen; the third endorsement indicates that the maker made a partial payment of $100 on April 15.

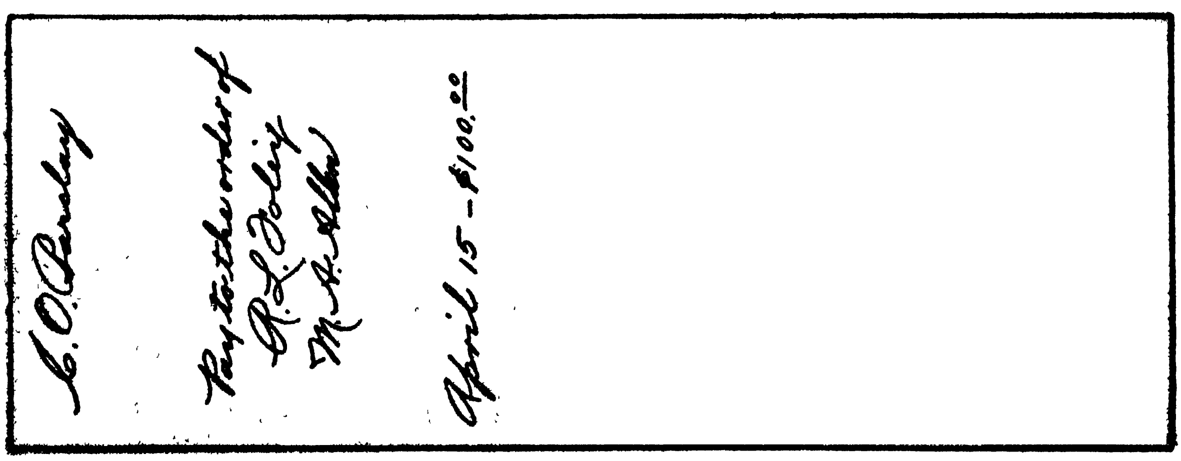


Illustration No. 42, Endorsements on Note

Dishonored Notes. Should the maker fail to pay or renew a note at maturity and it is not deemed collectible, the usual practice is to charge it to the reserve for bad debts account. Before making such an entry, however, every reasonable effort should be made to collect the principal and the accrued interest from the maker or any endorser. It should be remembered that each endorser is liable for the full amount of the note, plus any accrued interest. Assuming that A. W. Whitten failed to pay his note of May 29, which was a renewal of his note of March 30, and it is deemed uncollectible, it may be charged off by Wilson & Jones in the manner indicated in the following general journal entry:

Reserve for Bad Debts	$200.00	
Notes Receivable		$200.00
A. W. Whitten's dishonored note charged off.		

Sometimes a separate reserve for bad notes is provided, but usually the reserve for bad debts is intended to provide for losses on both accounts receivable and notes receivable.

Some accountants would advocate that the note be charged back to Mr. Whitten's account in order that his account might provide a complete history of the firm's dealings with him. While there are no objections to such a procedure, the same results may be accomplished by simply making a notation in Mr. Whitten's account to the effect that the note was not paid when due and that it has been charged off as a bad debt. Such information will be of value to the credit manager should Mr. Whitten seek additional credit at any time in the future.

Accounting for Notes Payable. The following types of transactions involve notes payable:

(a) Notes issued in exchange for merchandise or other property.
(b) Notes issued to creditors in order to obtain an extension of time on accounts payable.
(c) Notes issued as security for cash loans.
(d) Notes paid at maturity.
(e) Notes renewed at maturity.

Notes Issued in Exchange for Merchandise or Other Property. A note may be issued in exchange for merchandise, fixed assets, or other property. For example, Bryant & Wood issued a 30-day, 6 per cent interest-bearing note for $75 to the Modern Machine Co. in exchange for store equipment purchased on April 1. This transaction was recorded in the invoice record of Bryant & Wood by debiting Store Equipment, Account No. 21, and by crediting Notes Payable, Account No. 35, for $75. See page 341.

Notes Issued to Creditors in Order to Obtain an Extension of Time on Accounts Payable. When a firm wishes to obtain an extension of time on an account payable, a note for all or part of the amount due may be tendered to and accepted by the creditor. Assume, for example, that Bryant & Wood owe Williams & Co. $291.50 and by agreement on May 14 a check on the Liberty National Bank for $41.50 and a 90-day, 5 per cent interest-bearing note for $250 are issued. This transaction should be recorded in the books of Bryant & Wood as indicated by the following general journal entry:

May 14.	Accounts Payable	$291.50	
	Bank		$ 41.50
	Notes Payable		250.00
	Issued check for $41.50 and note for $250 to Williams & Co.		

Notes Issued as Security for Cash Loans. Many businesses experience periods in which receipts from customers in the usual course of business are not adequate to finance their operations. During such periods, therefore, it may be necessary to borrow money from banks. Business firms commonly borrow money from banks on short-term notes as an aid in financing their business operations. Assume, for example, that on May 15 Bryant & Wood borrow $1,000 from the Liberty National Bank on a 60-day, 6 per cent interest-bearing note. The transaction should be recorded as indicated in the following general journal entry:

May 15.	Bank	$1,000.00	
	Notes Payable		$1,000.00
	Borrowed $1,000 at the bank on a 60-day, 6% note.		

Notes Paid at Maturity. When a note payable matures, payment may be made direct to the holder or to a bank where it was left for collection. The maker will know who the payee is but he may not know who the holder is at maturity because the payee may have transferred the note to another party or he may have left it with a bank for collection. When a note is left with a bank for collection, it is customary for the bank to mail the maker a notice of maturity. For example, the Modern Machine Co. might forward the note of Bryant & Wood for $75 dated April 1 to the Liberty National Bank for collection and the bank might notify Bryant & Wood by sending them a notice similar to the one reproduced in Illustration No. 43.

If, upon receipt of this notice, Bryant & Wood issued a check to the bank for $75.38 in payment of the note and interest, the transaction

LIBERTY NATIONAL BANK

April 25, 19--

We hold a note signed by you on which there will be due on the 1st *day of* May *19--* *Principal $* 75.00

Interest $ .38

TOTAL $ 75.38

PLEASE BRING THIS NOTICE WITH YOU

To Bryant & Wood

542 S. Dearborn St., City

CHECKS ON OTHER BANKS NOT RECEIVED UNLESS CERTIFIED

Illustration No. 43, Notice of Maturity

should be recorded in their books as indicated by the following general journal entry:

May 1.	Notes Payable	$75.00	
	Interest Expense	.38	
	Bank		$75.38
	Paid note issued to the Modern Machine Co. April 1, plus interest.		

Notes Renewed at Maturity. If the maker is unable to pay a note in full at maturity, he may arrange to renew all or a part of it. For example, on August 12 Bryant & Wood might pay the interest, amounting to $3.13, and $50 on the principal of the note for $250 issued to Williams & Co. on May 14 and give them a new note for $200 with interest at 5 per cent payable in 60 days. This transaction should be recorded as indicated in the following general journal entry:

Aug. 12.	Notes Payable (old note)	$250.00	
	Interest Expense	3.13	
	Bank		$ 53.13
	Notes Payable (new note)		200.00
	Issued a check for $53.13 and a note for $200 to Williams & Co. in settlement of a note for $250 plus interest.		

Notes Payable Register. Where many notes are issued in the usual course of business, it may be advisable to keep an auxiliary record of such notes that will provide more detailed information than can be provided in a ledger account. Such an auxiliary record is usually known as a

NOTES PAYABLE REGISTER

DATE ISSUED		NO.	TO WHOM PAYABLE	WHERE PAYABLE		DATE MADE		
				BANK OR FIRM	ADDRESS	MO.	DAY	YEAR
19— Mar.	15	1	Dalton & Co	Union Bank	Springfield	Mar	15	19—
May	16	2	Woods Bros	City National Bank	Canton	May	16	19—
	20	3	City National Bank	" " "	City	May	20	19—
	22	4	Luce Motor Car Co	" " "	"	May	22	19—
	22	5	" " " "	" " "	"	May	22	19—
	29	6	City National Bank	" " "	"	May	29	19—

(Left-hand page)

notes payable register. One form of a notes payable register is reproduced above. The notes recorded in the illustration were those issued by Wilson & Jones during the period indicated by the record.

The information recorded in the register may be obtained directly from the note before it is mailed or given to the payee, or from a note stub. Blank notes are usually made up in pads with stubs attached on which spaces are provided for recording such essential information as Amount, Payee, Where Payable, Date, Time, Rate of Interest, and Number. The due date of each note is calculated and entered in the proper When Due column of the register. The interest at maturity is also calculated and entered in the Interest Amount column. When a note is paid, the date is entered in the Paid column.

Notes Payable Account. The information recorded in the notes payable account should agree with that recorded in the notes payable register. The following account contains a record of the notes that were entered in the notes payable register of Wilson & Jones. It should be noted that the identity of each note is indicated by the number of the note.

NOTES PAYABLE

19--			19--				
June 13	No. 1	150.00	Mar. 15	No. 1		150.00
			May 16	No. 2		378.65
			20	No. 3		1,000.00
			22	No. 4		200.00
			22	No. 5		200.00
			29	No. 6		2,500.00
					4,278.65	4,428.65

NOTES PAYABLE REGISTER

TIME	WHEN DUE J	F	M	A	M	J	J	A	S	O	N	D	AMOUNT	INTEREST RATE	INTEREST AMOUNT	PAID	REMARKS
90 ds.						13							150 00	—		June 13	
60 ds.							15						378 65	6%	3 79		
90 ds.								18					1000 00	6%	15 00		
3 mos.								22					200 00	6%	3 00		
6 mos.											22		200 00	6%	6 00		
60 ds.							28						2500 00	5%	20 83		

(Right-hand page)

Proving the Notes Payable Account. Periodically, usually at the end of each month, the notes payable account should be proved by comparing the balance of the account with the total notes outstanding as shown by the notes payable register. Following is a schedule of the notes outstanding on May 31:

SCHEDULE OF NOTES OUTSTANDING

No. 2	$ 378.65
No. 3	1,000.00
No. 4	200.00
No. 5	200.00
No. 6	2,500.00
Total	$4,278.65

It will be noted that the total of this schedule is the same as the balance of the notes payable account.

Accrued Interest. The value of an interest-bearing note increases daily because the maker has promised to pay the face of the note and the interest at maturity. This daily increase in value is known as accrued interest. Since interest may accrue on both notes receivable and notes payable, it is customary to keep two accounts, as follows, for use in recording accrued interest:

(a) Accrued Interest Receivable.

(b) Accrued Interest Payable.

Accrued Interest Receivable. While interest on notes receivable accrues daily, it is not practical to record the income until it is collected or until the accounts are adjusted at the close of an accounting period. Any interest collected during an accounting period should be recorded by debiting the bank account and by crediting Interest Income.

The accrued interest receivable account is an asset account that should be adjusted at the close of each accounting period so that the balance will be in agreement with the sum of the interest accrued on all notes owned at that time. Computing the interest accrued on notes receivable is similar in some respects to taking an inventory of merchandise or supplies. For example, if the unpaid notes recorded in the notes receivable register of Wilson & Jones represented all of the notes owned at the close of the year ended June 30, the procedure in adjusting the account with Accrued Interest Receivable would be as follows:

(a) Ascertain the balance of the accrued interest receivable account as of June 30. (For the purpose of this illustration it is assumed that the account had a debit balance of $4.20.)

(b) Compute the accrued interest on the unpaid notes owned on June 30 and prepare a schedule similar to the following:

SCHEDULE OF ACCRUED INTEREST ON NOTES RECEIVABLE

No.	Principal	Rate	Time	Amount
5	$350.00	6%	46 days	$2.68
6	286.50	6%	85 days	4.06
8	218.60	...	....	....
9	200.00	6%	32 days	1.07
Total accrued interest receivable				$7.81

(c) Since the interest accrued on notes receivable as of June 30 amounted to $7.81 and the account with Accrued Interest Receivable had a debit balance of only $4.20, it is necessary to adjust the account by debiting it for $3.61 in order to bring the balance into agreement with the schedule. The adjusting entry may be made in journal form as follows:

Accrued Interest Receivable	$3.61	
Interest Income		$3.61

Adjustment for increase in accrued interest receivable.

After this entry is posted, the account with Accrued Interest Receivable will have a debit balance of $7.81, which is the correct asset value of the account.

The adjusting entry required at the close of each accounting period to record accrued interest receivable depends on the following factors:

(a) The balance of the accrued interest receivable account before adjustment.

(b) The amount of the interest accrued on notes owned at the close of the period.

If the accrued interest is more than the debit balance of the accrued interest receivable account, the adjusting entry will involve a debit to Accrued Interest Receivable and a credit to Interest Income for the difference. If the accrued interest is less than the debit balance of the accrued interest receivable account, the adjusting entry will involve a debit to Interest Income and a credit to Accrued Interest Receivable for the difference.

Accrued Interest Payable. While interest on notes payable accrues daily, it is not practical to record the expense until it is paid or until the accounts are adjusted at the close of an accounting period. Any interest paid during an accounting period should be recorded by debiting Interest Expense and by crediting the bank account.

The accrued interest payable account is a liability account that should be adjusted at the close of each accounting period so that the balance will be in agreement with the sum of the interest accrued on all notes outstanding at that time. The procedure in adjusting the accrued interest payable account is similar to the procedure in adjusting the accrued interest receivable account. For example, if the unpaid notes recorded in the notes payable register of Wilson & Jones represent all of the notes outstanding at the close of the year ended June 30, the procedure in adjusting the account with Accrued Interest Payable would be as follows:

(a) Ascertain the balance of the accrued interest payable account as of June 30. (For the purpose of this illustration it is assumed that this account had a credit balance of $6.40.)

(b) Compute the accrued interest on the unpaid notes outstanding on June 30 and prepare a schedule similar to the one shown at the top of the following page.

(c) Since the interest accrued on notes payable as of June 30 amounted to $23.38 and the account with Accrued Interest Payable had a credit balance of only $6.40, it is necessary to adjust the account by crediting it for $16.98 in order to bring the balance into agreement with the schedule.

SCHEDULE OF ACCRUED INTEREST ON NOTES PAYABLE

No.	Principal	Rate	Time	Amount
2	$ 378.65	6%	45 days	$ 2.84
3	1,000.00	6%	41 days	6.83
4	200.00	6%	39 days	1.30
5	200.00	6%	39 days	1.30
6	2,500.00	5%	32 days	11.11
	Total accrued interest payable			$23.38

The adjusting entry may be made in journal form as follows:

Interest Expense	$16.98	
Accrued Interest Payable		$16.98
Adjustment for increase in accrued interest payable.		

After this entry is posted, the account with Accrued Interest Payable will have a credit balance of $23.38, which is the correct amount of this current liability.

The adjusting entry required at the close of each accounting period to record accrued interest payable depends on the following factors:

(a) The balance of the accrued interest payable account before adjustment.

(b) The amount of the interest accrued on notes outstanding at the close of the period.

If the accrued interest is more than the credit balance of the accrued interest payable account, the adjusting entry will involve a debit to Interest Expense and a credit to Accrued Interest Payable for the difference. If the accrued interest is less than the credit balance of the accrued interest payable account, the adjusting entry will involve a debit to Accrued Interest Payable and a credit to Interest Expense for the difference.

***PRACTICE ASSIGNMENT No. 29.** Complete Report No. 29 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 30 is required.*

XXX DRAFTS AND TRADE ACCEPTANCES

A draft is "an unconditional order in writing addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to order or to bearer."* There are two kinds of drafts as follows:

(a) Bank drafts.

(b) Commercial drafts.

Bank Drafts. A bank draft is a check drawn by a bank on funds that it has deposited in another bank. For example, a Chicago bank having funds deposited in a New York bank may draw against such funds by ordering the New York bank to pay a specified sum to a designated third party. Anyone may obtain a bank draft from a bank by paying the bank a sum equal to the amount of the desired draft plus the service charge. Illustration No. 44 is a reproduction of a bank draft drawn by the Liberty National Bank of Chicago, on the Chase National Bank of New York in favor of Bryant & Wood. Banks usually have funds on deposit in other banks located in other cities and can, therefore, issue bank drafts payable in such cities.

A bank draft differs from a cashier's check in that it is drawn on funds deposited in another bank. Both may be signed by the cashier of the

LIBERTY NATIONAL BANK 13-3/420

CHICAGO April 17, 19--

PAY TO THE ORDER OF Bryant & Wood $200.00

Two Hundred and no/100 - Dollars

To Chase National Bank
New York, N. Y.

[illegible]
Cashier.

Illustration No. 44, Bank Draft

*Uniform Negotiable Instruments Act.

bank that issues them. If it is a cashier's check, it is a draft on the bank drawing the draft. If it is a bank draft, it is a draft on another bank in which the drawer has funds on deposit.

If an ordinary check is issued in payment of a bank draft, it should be recorded in the usual manner. If it is issued in payment of a draft that is to be sent to a creditor in payment of his account, it should be recorded by debiting Accounts Payable for the amount of the draft, by debiting an expense account for the amount of any service charges, and by crediting the bank for the total amount of the check issued. One reason for using a bank draft in remitting to a creditor may be that the debtor is unknown to the creditor and has not established credit. Usually, ordinary checks will be accepted by a creditor, subject to payment upon presentation. However, ordinary checks may not be acceptable in the case of out-of-town cash purchases. In such cases bank drafts, cashier's checks, or certified checks may be used to advantage. All are negotiable instruments and the bank on which they are drawn is responsible for payment; hence the credit of the purchaser or debtor is not involved.

Commercial Drafts. A commercial draft is a formal demand by one party for payment by another party to a third party. The party making the demand is known as the *drawer;* the party on whom the draft is drawn is known as the *drawee;* and the party to whom the draft is payable is known as the *payee.* Usually the payee is a bank or other collecting agency for the drawer.

In both commercial drafts and bank drafts there are three parties involved — the drawer, the drawee, and the payee. In the case of a commercial draft the payee is usually a bank while the other parties are individuals or firms other than banks. In the case of a bank draft, the drawer and the drawee are banks while the payee is an individual or firm other than a bank.

There are three types of commercial drafts as follows:

(a) Sight drafts.
(b) Time drafts.
(c) Trade acceptances.

Sight Drafts. A commercial draft that is made payable upon presentation is known as a *sight draft.* It indicates that the amount is either due or past due and that the drawer is demanding payment at once. A model filled-in copy of a sight draft is reproduced in Illustration No. 45. The

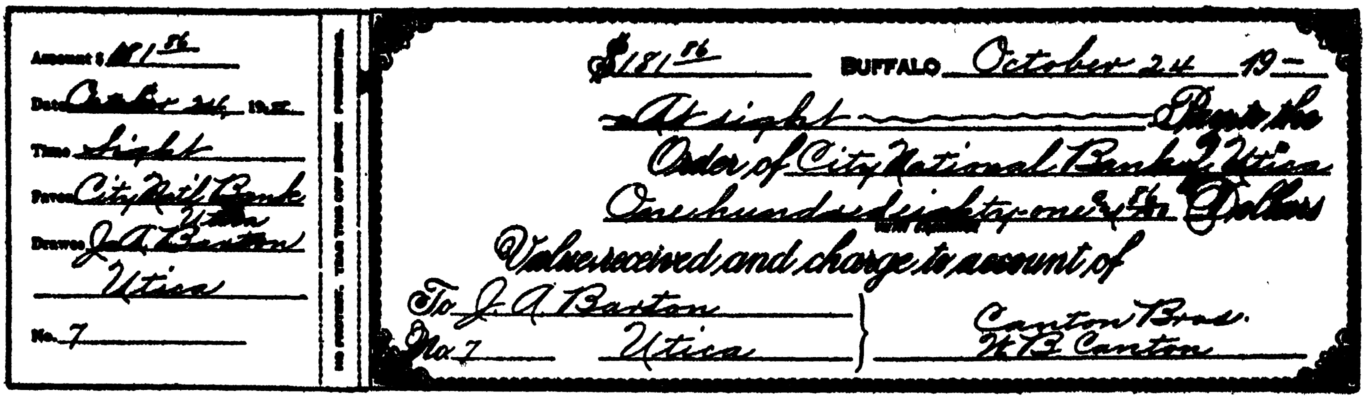


Illustration No. 45, Sight Draft with Stub

drawer of this draft is Canton Bros.; the drawee is J. A. Barton; and the payee is the City National Bank of Utica. It should be noted that the draft is payable at sight. While a draft is a demand for payment, the drawee is not required to honor it upon presentation. If the draft is honored upon presentation, it must be paid at once. If Mr. Barton refuses payment upon presentation, the draft is said to be dishonored and it will then be returned to the drawer by the bank with a statement to the effect that Mr. Barton refused to honor it.

A sight draft does not constitute a written promise "to pay a sum certain in money" until it is accepted by the drawee. If it is accepted, it must be paid immediately, since it is payable on sight. Accounting for sight drafts, therefore, differs from accounting for other negotiable instruments. A memorandum record is ordinarily all that is required at the time a sight draft is drawn. This record may be a stub of the draft, similar to the stub attached to the sight draft reproduced in Illustration No. 45, or it may be a notation in the ledger account of a customer on whom a sight draft is drawn. If the draft is dishonored, a notation to this effect should be made either on the stub of the original draft or in the ledger account. It should be noted that the accounts of the drawer are not affected either by the drawing of a sight draft or by the failure of the drawee to honor it. On the other hand, if the drawee accepts the draft by paying it at sight, the drawer will in due time receive a remittance from the bank to whom it was made payable. Upon receipt of this remittance, an entry should be made in the books of the drawer debiting the bank account for the amount of the remittance received, debiting Collection Expense for the amount of the bank's service charge, and crediting Accounts Receivable for the amount of the draft.

The most common uses of sight drafts are as follows:

(a) To aid in collecting accounts receivable.

(b) To facilitate the handling of C.O.D. freight shipments.

Before a draft is drawn as a collection device, it is customary to obtain permission from the drawee to draw the draft. Permission may be requested in advance, or the drawee may be notified that unless payment of an account is made by a specified date, a sight draft will be drawn. In either case the drawee is notified in advance that a sight draft may be drawn on him. When the draft is drawn, it is usually made payable to a bank located in the same city as the drawee. The bank is instructed to present the draft and to remit the proceeds. When the draft is presented, the drawee must either pay it immediately or refuse to pay it. Refusal to pay the draft may be embarrassing to a person who wants to maintain a good credit record. A debtor who enjoys a high credit rating with his bank and with his creditors is seldom confronted with a sight draft. Should a sight draft be drawn on him by mutual agreement, he will have no hesitancy in accepting it by paying it at sight.

Order Bill of Lading — Sight Draft Attached. A simple method of handling C.O.D. freight shipments was discussed in Unit Twelve. Some firms prefer to make such C.O.D. freight shipments by means of an *order bill of lading* with a sight draft attached. Under this plan title to the

EUREKA TIRE & RUBBER COMPANY
246 DEVONSHIRE STREET
CLEVELAND, OHIO

DIRECTORS
HUBERT L. CARTER, TREAS.
GEORGE H. LOWE, PRES.
JOHN C. KENNEDY SECY.
C. A. YOUNG
F W POWER
W L CARTER
E. A. CARTER
W. H. DUNBAR

No. C 2393

DATE August 14, 19--
YOUR ORDER A 3517
OUR ORDER 875
SALESMAN Reid

Sold to Bryant & Wood
542 S. Dearborn St.
Chicago, Ill.

VIA C.C.C. & ST. L. R.R. TERMS C.O.D.

	Description	Quantity Ordered	Quantity Shipped	Excise Tax	Unit Price	Extension	Total
6.00-16	4-Ply Safety Tires	12	12	1.12	11.46	137.52	
6.70-15	4-Ply DeLuxe Tires	12	12	1.19	12.57	150.84	
6.50-16	4-Ply Safety Tires	12	12	1.24	14.14	169.68	
6.00-16	Heavy Duty Tubes	18	18	.24	1.80	32.40	490.44
					Federal excise tax		46.92
					Total		537.36

Illustration No. 46, C.O.D. Purchase Invoice

$ 537.36 CLEVELAND August 14, 19--

------ At Sight ------------------------ Pay to the

Order of First National Bank, Chicago, Illinois

Five hundred thirty-seven and 36/100 ---------------------- Dollars

WITH EXCHANGE

Value received and charge the same to account of

To Bryant & Wood

No. 21 Chicago, Illinois

EUREKA TIRE & RUBBER CO.

C. H. Tallent

Illustration No. 47, Sight Draft

property covered by the bill of lading does not pass to the buyer until he surrenders the original copy and obtains possession of the property. The order bill of lading instructs the freight agent at the destination to hold the merchandise until the original copy of the bill of lading has been presented by the consignee. At the time of making shipment the shipper draws a sight draft for the amount of the invoice and attaches to it the original copy of the order bill of lading. The draft is made payable to a bank located in the same city as the consignee. The bill of lading is transferred to this bank by endorsement, and both the draft and the original copy of the bill of lading are mailed to the bank.

Upon receipt of the draft and the order bill of lading, the bank presents the draft to the consignee for payment. After paying the draft, the consignee will be given the original copy of the order bill of lading. By presenting this bill of lading to the freight agent he may then obtain the property consigned to him. In handling this transaction the bank acts as an agent of the seller or consignor and collects the amount specified in the draft before delivering the bill of lading to the consignee.

To illustrate the use of the order bill of lading, it is assumed that Bryant & Wood placed a purchase order with the Eureka Tire & Rubber Co., shipment to be made by freight, C.O.D. Upon receipt of the order, the Eureka Tire & Rubber Co. billed the merchandise ordered and mailed the original copy of the invoice to Bryant & Wood so that they would know the amount. The purchase invoice received by Bryant & Wood is reproduced in Illustration No. 46.

At the time of making shipment, the Eureka Tire & Rubber Co. drew a sight draft on Bryant & Wood for the amount of the invoice and mailed this draft to the First National Bank of Chicago with the original copy of the order bill of lading attached. The draft is reproduced in Illus-

Uniform Domestic Straight Bill of Lading, adopted by Carriers in Official, Southern, Western and Illinois Classification Territories, March 15, 1922, as amended August 1, 1930 and June 15, 1941

UNIFORM ORDER BILL OF LADING
ORIGINAL

Shipper's No. ....

THE NEW YORK CENTRAL RAILROAD Company Agent's No. ....

RECEIVED, subject to the classifications and tariffs in effect on the date of issue of this Bill of Lading.

At Cleveland August 14, 19-- From Eureka Tire & Rubber Company

the property described below in apparent good order, except as noted (contents and condition of contents of packages unknown), marked, consigned, and destined as indicated below, which said company (the word company being understood throughout this contract as meaning any person or corporation in possession of the property under the contract) agrees to carry to its usual place of delivery at said destination, if on its own road or its own water line, otherwise to deliver to another carrier on the route to said destination. It is mutually agreed, as to each carrier of all or any of said property over all or any portion of said route to destination, and as to each party at any time interested in all or any of said property, that every service to be performed hereunder shall be subject to all the conditions not prohibited by law, whether printed or written, herein contained, including the conditions on back hereof, which are hereby agreed to by the shipper and accepted for himself and his assigns.

The surrender of this Original ORDER Bill of Lading properly indorsed shall be required before the delivery of the property. Inspection of property covered by this bill of lading will not be permitted unless provided by law or unless permission is indorsed on this original bill of lading or given in writing by the shipper.

Consigned to ORDER OF Eureka Tire & Rubber Co., 246 Devonshire St., Cleveland, Ohio

Destination Chicago State of Ill. County of Cook

Notify J. A. Bryant

At 542 S. Dearborn St., Chicago State of Ill. County of Cook

Route NYC

Delivering Carrier NYC Car Initial .... Car No. ....

NO PACKAGES	DESCRIPTION OF ARTICLES, SPECIAL MARKS AND EXCEPTIONS	* WEIGHT (Subject to Correction)	CLASS or RATE	CHECK COLUMN
20	bundles, 54 Tires	800#		

Subject to Section 7 of conditions, if this shipment is to be delivered to the consignee without recourse on the consignor, the consignor shall sign the following statement:

The carrier shall not make delivery of this shipment without payment of freight and all other lawful charges.

D. A. Brown
Signature of Consignor

If charges are to be prepaid, write or stamp here. "To be Prepaid."

Received $............

to apply in prepayment of the charges on the property described hereon.

Agent or Cashier

Per ....

(The signature here acknowledges only the amount prepaid.)

Charges Advanced:

$............

*If the shipment moves between two ports by a carrier by water, the law requires that the bill of lading shall state whether it is "carrier's or shipper's weight."

Note.—Where the rate is dependent on value, shippers are required to state specifically in writing the agreed or declared value of the property

The agreed or declared value of the property is hereby specifically stated by the shipper to be not exceeding $............ per ....

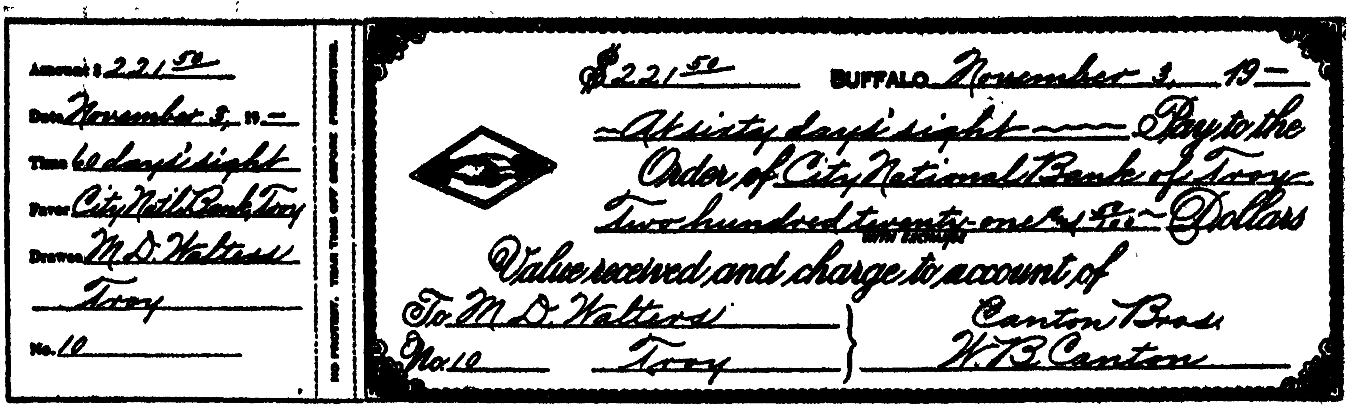
EUREKA TIRE & RUBBER CO. Shipper, Per D. A. B. AGENT .... PER 1

Permanent postoffice address of shipper .... Cleveland

Illustration No. 48, Order Bill of Lading

tration No. 47 and the original copy of the order bill of lading is reproduced in Illustration No. 48. It will be noted that the merchandise is consigned to the order of the Eureka Tire & Rubber Co. It was necessary, therefore, for the shipper to endorse the bill of lading before mailing it to the First National Bank of Chicago.

Time Drafts. A commercial draft that is made payable at a fixed or determinable future time is known as a *time draft.* It indicates that the amount is not yet due or that the drawer is willing to allow additional time in which to make payment. When accepted, a time draft becomes a negotiable instrument.


Amount $221 50/100
Date November 3, 19—
Time 60 days' sight
Payee City Nat'l Bank Troy
Drawee M. D. Walters
Troy
No. 10

$221 50/100 BUFFALO November 3, 19—
At sixty days' sight Pay to the
Order of City National Bank of Troy
Two hundred twenty-one 50/100 Dollars
WITH EXCHANGE
Value received and charge to account of
To M. D. Walters } Canton Bros.
No. 10 Troy } W. B. Canton

Illustration No. 49, Time Draft with Stub

Time drafts may be made payable as follows:

(a) On a specified date.
(b) At a specified number of days after sight.
(c) At a specified number of days after date.

If a time draft is made payable on a specified date, it becomes a negotiable instrument when accepted by the drawee and will be due on the date specified.

If a time draft is made payable at 30 days after sight, it becomes a negotiable instrument when accepted and will be due 30 days after the date of acceptance.

If a time draft is made payable at 30 days after date, it becomes a negotiable instrument when accepted and will be due 30 days after the date of the draft.

The time draft reproduced in Illustration No. 49 is payable 60 days after sight. After the draft was drawn, it was removed from the stub and sent to the City National Bank of Troy, the payee, with instructions to present it to M. D. Walters, the drawee, for acceptance. When the bank presented the draft to the drawee, he accepted it by writing his acceptance across the face and adding his signature as shown in Illustration No. 50. This procedure is sometimes referred to as honoring the draft. When Canton Bros. received the honored draft from the City National Bank of

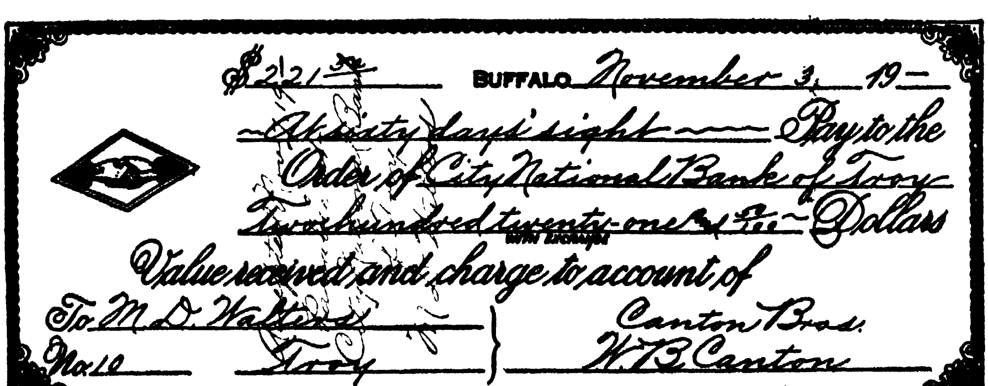

$221 50/100 BUFFALO November 3, 19—
At sixty days' sight Pay to the
Order of City National Bank of Troy
Two hundred twenty-one 50/100 Dollars
WITH EXCHANGE
Value received and charge to account of
To M. D. Walters } Canton Bros.
No. 10 Troy } W. B. Canton

Illustration No. 50, Honored Time Draft

Troy, they recorded the draft in the same manner as if it had been a 60-day noninterest-bearing note. Thus the transaction was recorded by debiting Notes Receivable and by crediting Accounts Receivable for $221.50. Had Mr. Walters refused to accept the draft, the bank would have returned it to Canton Bros. with a notation to the effect that it had been dishonored.

An auxiliary record of time drafts may be kept in note registers in the same manner as notes receivable and notes payable. An accepted time draft involves the same obligation as a note payable on the part of the drawee and is the same as a note receivable on the part of the drawer.

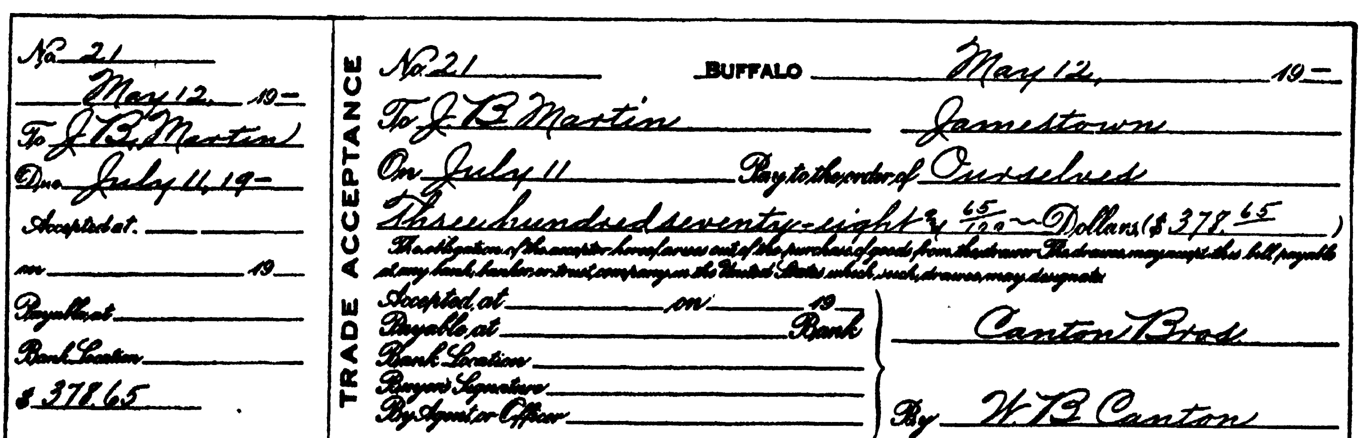
Trade Acceptances. A trade acceptance is similar to a time draft. It is a formal demand on the drawee by the drawer for the payment of a specified amount at a fixed or determinable future time. Its use is limited to transactions arising out of the purchase of goods. When accepted, it becomes a negotiable instrument that is similar to a note. The drawer of a trade acceptance may designate any bank or trust company as the payee, or the trade acceptance may be made payable direct to the drawer. The trade acceptance reproduced in Illustration No. 51 is made payable to the drawer.

Following are some of the advantages claimed for trade acceptances:

(a) They are self-liquidating. They arise out of the purchase of merchandise and it is assumed that the proceeds of the sales will provide the funds with which to pay the acceptances when they mature.

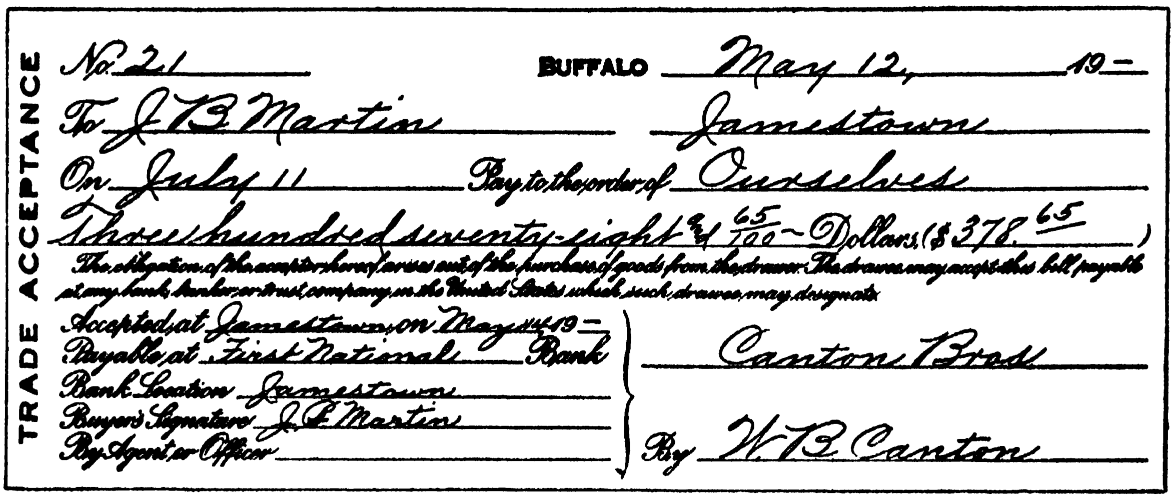
(b) Trade acceptances receivable possess the same legal status as notes receivable; hence they are preferable to open accounts receivable.

(c) The use of trade acceptances relieves a merchant of the burden of financing his customers through extending credit on open account. If necessary, trade acceptances can be discounted at a bank more readily and with less expense than accounts receivable may be assigned.


No. 21
May 12, 19—
To J. B. Martin
Due July 11, 19—
Accepted at
on 19
Payable at
Bank Location
$ 378.65

TRADE ACCEPTANCE
No. 21 BUFFALO May 12, 19—
To J. B. Martin Jamestown
On July 11 Pay to the order of Ourselves
Three hundred seventy-eight & 65/100 Dollars ($ 378.65)
The obligation of the acceptor hereof arises out of the purchase of goods from the drawer. The drawee may accept this bill payable at any bank, banker or trust company in the United States which such drawee may designate.
Accepted at on 19
Payable at Bank
Bank Location
Buyer's Signature
By Agent or Officer
Canton Bros.
By W. B. Canton

Illustration No. 51, Trade Acceptance with Stub


TRADE ACCEPTANCE

No. 21 BUFFALO May 12, 19—

To J. B. Martin Jamestown

On July 11 Pay to the order of Ourselves

Three hundred seventy-eight & 65/100 Dollars ($378.65)

The obligation of the acceptor hereof arises out of the purchase of goods from the drawer. The drawee may accept this bill payable at any bank, banker or trust company in the United States which such drawee may designate.

Accepted at Jamestown on May 14 19—

Payable at First National Bank

Bank Location Jamestown

Buyer's Signature J. B. Martin

By Agent or Officer

Canton Bros.

By W. B. Canton

Illustration No. 52, Honored Trade Acceptance

(d) Experience indicates that the loss on trade acceptances will be less than on open accounts receivable.

When merchandise is sold on trade acceptance terms, it is customary to bill the merchandise in the usual way, indicating that the terms are "trade acceptance." The sales invoice is recorded in the usual manner by debiting Accounts Receivable and by crediting Sales. A trade acceptance is drawn on the customer and is attached to the sales invoice. The following transactions and illustrations will explain the procedure more fully:

May 12. Canton Bros., Buffalo, sold merchandise to J. B. Martin, Jamestown, amounting to $378.65; terms, 60-day trade acceptance.

May 15. Canton Bros. received from J. B. Martin the honored trade acceptance reproduced in Illustration No. 52.

The merchandise was billed and the sales invoice was recorded in the sales journal in the same manner as other charge sales. The trade acceptance reproduced in Illustration No. 51 was prepared and attached to the invoice, both being mailed to J. B. Martin. A carbon copy of the sales invoice was used for posting purposes, J. B. Martin's account in the accounts receivable ledger being debited for the amount of the sale and the terms being indicated in the Items column.

The honored trade acceptance was recorded in the manner indicated in the following general journal entry:

Notes Receivable..............................	$378.65	
Accounts Receivable..........................		$378.65
Received a trade acceptance from J. B. Martin.		

The trade acceptance was also entered in the notes receivable register of Canton Bros.

When J. B. Martin received the sales invoice from Canton Bros., he honored the trade acceptance and recorded the transaction in his invoice record by debiting Purchases and by crediting Notes Payable. If preferred, the invoice may be recorded in the invoice record in the same manner as other credit purchases and the trade acceptance may be recorded in the general journal by debiting Accounts Payable and by crediting Notes Payable.

PRACTICE ASSIGNMENT No. 30. Complete Report No. 30 in the workbook and submit your working papers to your instructor for approval. Then continue with the next study assignment in Unit Fifteen until Report No. 31 is required.

Unit Fifteen

ACCOUNTING FOR SUPPLIES, PREPAID ITEMS, AND FIXED ASSETS

XXXI SUPPLIES AND PREPAYMENTS

Office supplies, store supplies, advertising materials, fuel, and other supplies may be purchased during an accounting period but may not be wholly consumed in the same period. The premium on insurance covering merchandise, equipment, and buildings may be prepaid, but the term of the policy may extend beyond the accounting period in which the service was contracted for. Rent and interest may be paid in advance, but the expense may not be wholly incurred in the same accounting period. The cost of unused supplies on hand at the close of an accounting period and of prepaid items not incurred during the accounting period should be treated as current assets. Such items represent temporary assets that will become expenses in the period in which they are consumed or used.

When the accounts are kept on the accrual basis, it is necessary to adjust certain accounts at the close of each accounting period for the following:

(a) The amounts of any supplies or services purchased during the period that were recorded as assets at time of purchase and that were consumed or used during the period.

(b) The amounts of any supplies or services purchased during the period that were recorded as expenses at time of purchase and that were not consumed or used during the period.

Asset Method of Accounting for Supplies and Prepayments. Supplies, such as office supplies, store supplies, advertising supplies, fuel, and postage, that may be purchased in one accounting period but may not be wholly consumed in the same period are usually recorded as assets at the time of purchase.

Office Supplies. Office supplies may consist of letterheads and envelopes, pencils and pen holders, carbon paper, ink, notebooks, typewriter ribbons, rubber bands, paper clips, and other miscellaneous supplies that are normally consumed in the operation of an office. Transactions arising from the purchase of such supplies on credit should be entered in the invoice record. When such supplies are purchased for cash, the transactions should be entered in the record of checks issued. In either case the purchases are posted to an account with Office Supplies in the general ledger.

At the end of each accounting period an inventory of the unused office supplies on hand is taken and an adjusting entry is made to record the amount of the office supplies consumed during the period. For example, if on December 31 the office supplies account has a debit balance of $300 and an inventory reveals that the value of the supplies on hand amounts to $100, it is apparent that the supplies consumed during the period amounted to $200. The required adjustment may be made as indicated in the following general journal entry:

Office Supplies Consumed	$200.00	
Office Supplies		$200.00
Office supplies consumed during period.		

After this entry is posted, the office supplies account will have a debit balance of $100, which should be listed in the balance sheet as a current asset. The account with Office Supplies Consumed will have a debit balance of $200, which should be listed in the profit and loss statement as an operating expense.

Store Supplies. Store supplies may consist of wrapping paper and twine, corrugated board, paper bags and other containers, cleaning supplies, and other miscellaneous supplies that are normally consumed in the operation of a store. Transactions arising from the purchase of such supplies should be recorded in the same manner as transactions arising from the purchase of office supplies; that is, purchases should be recorded by debiting Store Supplies and by crediting Accounts Payable or the bank account, depending upon whether they are purchased on credit or for cash.

At the end of each accounting period an inventory of the unused store supplies on hand is taken and an adjusting entry is made to record the amount of the store supplies consumed during the period. The method of adjusting the store supplies account is the same as the method of adjusting the office supplies account.

For example, if on December 31 the store supplies account has a debit balance of $240 and an inventory reveals that the value of the supplies on hand amounts to $70, it is apparent that the supplies consumed during the period amounted to $170. The required adjustment may be made as indicated in the following general journal entry:

Store Supplies Consumed	$170.00	
Store Supplies		$170.00
Store supplies consumed during period.		

After the adjusting entry is posted, the debit balance of the store supplies account represents an asset that should be listed in the balance sheet as a current asset. At the same time the debit balance of the account with Store Supplies Consumed represents an expense that should be listed in the profit and loss statement as an operating expense.

Advertising Supplies. Advertising supplies may consist of catalogs, circulars, price lists, order blanks, and other miscellaneous supplies that are normally consumed in the advertising program. Transactions arising from the purchase of such supplies should be recorded in the same manner as transactions arising from the purchase of other supplies; that is, purchases should be recorded by debiting Advertising Supplies and by crediting Accounts Payable or the bank account, depending upon whether they are purchased on credit or for cash.

At the end of each accounting period an inventory of the unused advertising supplies on hand is taken and an adjusting entry is made to record the amount of the advertising supplies consumed during the period. The method of adjusting the advertising supplies account is the same as the method of adjusting the office supplies and store supplies accounts.

For example, if on December 31 the advertising supplies account has a debit balance of $375 and an inventory reveals that the value of the supplies on hand amounts to $125, it is apparent that the supplies consumed during the period amounted to $250. The required adjustment may be made as indicated in the following general journal entry:

Advertising Supplies Consumed	$250.00	
Advertising Supplies		$250.00
Advertising supplies consumed during period.		

After the adjusting entry is posted, the debit balance of the advertising supplies account represents an asset that should be listed in the balance sheet as a current asset. At the same time the debit balance of the account with Advertising Supplies Consumed represents an expense that should be listed in the profit and loss statement as an operating expense.

Postage Stamps. The value of postage stamps purchased is usually recorded by debiting Postage Stamps and by crediting the bank account. Usually a check is made payable to Postage and, after it is cashed at the bank, the money is used to purchase stamps in the desired denominations. Some of the stamps may be used on parcel-post packages and the balance on ordinary mail. A memorandum record of the stamps used on parcel-post packages may be kept until the end of the month, when the total is recorded by debiting Transportation Out and by crediting Postage Stamps. Usually no record is kept of the stamps used on ordinary mail each day, but periodically the unused stamps are counted and their total value is ascertained. The difference between the value of the unused stamps on hand and the debit balance of the postage stamps account represents the value of the stamps used on ordinary mail.

If the account with Postage Stamps is debited (a) for the value of the stamps on hand at the beginning of the month, \$15, and (b) for the amount of stamps purchased during the month, \$85, and is credited for the value of the stamps used on parcel-post packages during the month, \$40, the account will have a debit balance of \$60 at the end of the month. If, at that time, the value of the unused stamps on hand is found to be \$25, the difference, or \$35, represents the value of the stamps that must have been used on ordinary mail during the month. It is therefore necessary to adjust the accounts in order to record the decrease in the asset Postage Stamps to an amount that is in agreement with the inventory of unused stamps and to record the increase in postage expense resulting from the stamps used on ordinary mail during the month. The required adjustment may be made as indicated in the following general journal entry:

Postage....................................	\$35.00	
Postage Stamps..............................		\$35.00
Value of stamps used on ordinary mail.		

After the adjusting entry is posted, the account with Postage Stamps will have a debit balance of \$25, which represents an asset that should be listed in the balance sheet as a current asset. The account with Postage will have a debit balance of \$35, representing an expense that should be listed in the profit and loss statement as an operating expense.

In addition to buying postage stamps, a firm may make a deposit under the permit system that entitles it to a certain amount of postage. Sometimes postage meters are used. In this case, a certain amount of postage is paid for and the meter is set so that a certain amount of postage may be used as needed. Regardless of whether postage stamps are purchased, whether a deposit is made under the permit system, or whether metered postage is purchased, the accounting procedure may be the same. The prepaid postage may be charged to an account with postage stamps, and when the stamps are used or the postage is consumed, the amount should be charged to the proper expense accounts.

Insurance. Insurance against loss from fire, water, windstorm, burglary, and other casualties is a form of protection provided by insurance companies. A contract under which an insurance company, the insurer, agrees to protect the owner of property, the insured, from loss on such property is known as an *insurance policy.* The amount that the insured is required to pay for such protection is known as the *premium.* The premium is usually stated as a specified rate per $1,000 of insurance for one or more years. If the rate is quoted on a basis of one year, it is known as the *annual rate.* If it is quoted for a longer period than one year, it is known as the *term rate.* Since insurance is usually purchased for a period of one or more years and the premium must be paid in advance by the policyholder, the amount paid is usually charged to an account with Prepaid Insurance, which is classified as a current asset account.

Expired Insurance. The asset value of prepaid insurance decreases day by day, but it is not customary to keep a daily record of expired insurance. Instead the usual plan is to record, at the close of each accounting period, the total amount of expired insurance applicable to each period. Thus an entry may be made at the end of each month to record the amount of the insurance expired during the month.

Many firms keep an auxiliary record of insurance policies similar to the one reproduced on pages 424 and 425. The left-hand page is used to record the essential information with respect to each policy. It also provides the information needed in distributing the insurance premium on each policy in the columns provided on the right-hand page. To ascertain the amount of the expired premium to be entered in the column provided for each month, it is only necessary to divide the total premium by the number of months in the term of the policy. Thus, if the premium amounts to $15 and the term of the policy is one year, the amount of insurance expired monthly will be $1.25 ($15 ÷ 12 months). The total of each monthly column is the amount of insurance expired during the month. Before this amount can be recorded, it is necessary to make a proper distribution of the insurance expense. It will be noted that the total insurance expired during the month of December amounted to $13.75,

INSURANCE POLICY REGISTER

DATE OF POLICY		POLICY NO.	NAME OF INSURANCE COMPANY	PROPERTY INSURED	AMOUNT OF INSURANCE	TERM	PREMIUM
19– June	1	16431A	Union Fire & Theft Ins. Co	Truck Fire & Theft	1,000 00	1 yr.	15 00
	1	67231	Merchants Ins. Co	Truck Property Damage	1,000 00	1 yr.	45 00
	1	664218	Globe Ins. Co.	Merchandise	5,000 00	1 yr.	45 00
	1	94109	U. S. Fire Ins. Co	Office Equipment	2,000 00	1 yr.	43 20
July	1	92368	Standard Ins. Co.	Merchandise	5,000 00	1 yr.	45 00
Nov.	1	369810	National Ins. Co.	Store Equipment	1,000 00	1 yr.	15 00

(Left-hand page)

The insurance expired during December was distributed as follows:

Expired insurance on merchandise	$ 7.50
Expired insurance on delivery equipment	5.00
Expired insurance on store equipment	1.25
Total	$13.75

INSURANCE POLICY REGISTER

DATE OF POLICY		POLICY NO.	NAME OF INSURANCE COMPANY	PROPERTY INSURED	AMOUNT OF INSURANCE	TERM	PREMIUM
19– June	1	16431A	Union Fire & Theft Ins. Co	Truck Fire & Theft	1,000 00	5 mos.	6 25
	1	67231	Merchants Ins. Co	Truck Property Damage	1,000 00	5 mos.	18 75
	1	664218	Globe Ins. Co	Merchandise	5,000 00	5 mos.	18 75
July	1	92368	Standard Ins. Co	"	5,000 00	6 mos.	22 50
Nov.	1	369810	National Ins. Co	Store Equipment	1,000 00	10 mos.	12 50

(Left-hand page)

INSURANCE POLICY REGISTER

JAN.	FEB.	MAR.	APR.	MAY	JUNE	JULY	AUG.	SEPT.	OCT.	NOV.	DEC.	EXPIRED	UNEXPIRED
					1 25	1 25	1 25	1 25	1 25	1 25	1 25	8 75	6 25
					3 75	3 75	3 75	3 75	3 75	3 75	3 75	26 25	18 75
					3 75	3 75	3 75	3 75	3 75	3 75	3 75	26 25	18 75
					3 60	3 60	3 60	12 40	(Cancelled Aug 31)			23 20	
					[illegible]	3 75	3 75	3 75	3 75	3 75	3 75	22 50	22 50
						[illegible]	[illegible]	[illegible]	[illegible]	1 25	1 25	2 50	12 50
										[illegible]	[illegible]	[illegible]	[illegible]

(Right-hand page)

The amount of the expired insurance was therefore recorded as indicated by the following general journal entry:

Expired Insurance on Merchandise	$7.50	
Expired Insurance on Delivery Equipment	5.00	
Expired Insurance on Store Equipment	1.25	
Prepaid Insurance		$13.75
Insurance expired during December.		

After the expired insurance is recorded for each month during the year, the balance of the prepaid insurance account at the end of the year should be the same as the total of the unexpired insurance premium column in the insurance policy register.

At the beginning of each year, it is necessary to forward the data in the insurance policy register as shown in the illustration at the bottom of page 424. The left-hand page only of the register is reproduced in this illustration. In bringing forward the data, the unexpired term of the policy and the amount of the unexpired premium are recorded; thus the information needed in computing the amount of the premium to be charged off each month is available. For example, the unexpired premium on Policy No. 16431A amounted to $6.25 and the policy had five months to run; therefore, one fifth of the unexpired premium, or $1.25, should be charged off during each of the next five months. The unexpired premium on Policy No. 92368 amounted to $22.50 and the policy had six months to run; therefore, one sixth of the unexpired premium, or $3.75, should be charged off during each of the next six months.

The premiums on all the other policies should be distributed in like manner. At the time of forwarding the amount of unexpired insurance to a new page, the total of the Premium column should be in agreement with the debit balance of the prepaid insurance account.

Canceled Insurance. A policyholder has the privilege of canceling the insurance at any time before expiration of the policy. If a policy is canceled, the insured is entitled to receive a refund for that part of the premium applicable to the unexpired period. In computing the amount of the refund, however, it is customary to charge a higher rate, known as the *short-term rate,* for the expired period. In other words, if a policy is canceled before it expires, the insured is charged a higher rate of premium for the period already expired than that charged when the policy was originally issued. To record the amount refunded, it is only necessary to debit the bank account and to credit the prepaid insurance account. At the same time an entry should be made in the insurance policy register to indicate that the policy was canceled and to record the additional cost of insurance due to the short-term rate charged. This increased cost should be recorded in the column for the month in which the refund was received.

Policy No. 90169, purchased on June 1, was canceled on August 31. The insurance company refunded $20 in September and the loss of $12.40, representing the difference between the short-term rate and the annual rate, was recorded in the September column. It could not be recorded in the August column because the amount of the loss was not known until the amount of the refund was received in September.

Prepaid Interest. Sometimes interest is prepaid on a note payable. When this is done and the note does not mature in the same accounting period, the amount of interest paid may be recorded as a charge to a prepaid interest account which should be classified as a current asset account.

At the end of the accounting period the amount of the interest expense actually incurred during the period should be calculated and an adjusting entry should be made to transfer that portion of the interest from the prepaid interest account to an interest expense account. For example, on December 1 a note for $1,000 due in three months with interest at 6 per cent was issued to a bank and the interest amounting to $15 was paid in advance. On December 31 it was ascertained that one third of the interest expense was incurred during the current accounting period; therefore an adjustment was made as indicated in the following general journal entry:

Interest Expense..................................	$5.00	
Prepaid Interest................................		$5.00
Prepaid interest transferred to Interest Expense.		

After this entry was posted, the prepaid interest account had a debit balance of $10, which should be listed in the balance sheet as a current asset. The debit balance of the interest expense account should be listed in the profit and loss statement under the heading of "Other Charges."

Expense Method of Accounting For Supplies and Prepayments. Supplies and services that may not be wholly consumed in the period in which they are purchased may be recorded as expenses at the time of purchase. Under this method of accounting, it is necessary to adjust the accounts at the end of each accounting period in order that the unused portions may be recorded as assets. For example, if Office Supplies is classified as an expense account and during the period it is charged for a total of $200 and an inventory taken at the end of the period shows that there are supplies on hand amounting to $75, it will be necessary to adjust the accounts as indicated by the following general journal entry:

Unused Office Supplies	$75.00	
Office Supplies		$75.00
Office supplies on hand.		

After this entry is posted, the office supplies account will have a debit balance of $125 that should be listed in the profit and loss statement as an operating expense. The account with Unused Office Supplies will have a debit balance of $75 that should be listed in the balance sheet as a current asset.

A detailed comparison of the asset and expense methods of accounting for supplies and prepaid items is shown in parallel columns on the following page.

The final results are the same under both methods of accounting, but the adjusting entries required at the close of each accounting period differ. Under the asset method, adjusting entries are made periodically to record the amounts consumed or used during the period; under the expense method, entries are made periodically to record the asset value of the amounts to be deferred to a succeeding accounting period. Regardless of which method is used in accounting for supplies and prepaid items, it is advisable to follow a consistent policy.

PRACTICE ASSIGNMENT No. 31. Complete Report No. 31 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 32 is required.

Accounting for Prepaid Expenses

TRANSACTION. March 1. Purchased office supplies, $200. Terms, 30 days.

Asset Method

JOURNAL ENTRY

Mar. 1.	Office Supplies....	$200	
	Accounts Payable		$200
	Purchased office supplies on credit.		

Expense Method

JOURNAL ENTRY

Mar. 1.	Office Supplies....	$200	
	Accounts Payable		$200
	Purchased office supplies on credit.		

ADJUSTMENT DATA. December 31. Inventory of unused office supplies on hand, $75.

Asset Method

JOURNAL ENTRY

Dec. 31.	Office Supplies Consumed...........	$125	
	Office Supplies.		$125
	Office supplies consumed during period.		

Expense Method

JOURNAL ENTRY

Dec. 31.	Unused Office Supplies.............	$75	
	Office Supplies.		$75
	Unused office supplies on hand.		

Asset Method

LEDGER ACCOUNTS

OFFICE SUPPLIES (An asset account)

Mar. 1	*75*	200	Dec. 31	125

OFFICE SUPPLIES CONSUMED (An expense account)

Dec. 31	125		

ACCOUNTS PAYABLE

		Mar. 1	200

The balance of the account with Office Supplies amounting to $75 should be listed as a current asset in the balance sheet, while the balance of the account with Office Supplies Consumed amounting to $125 should be listed as an operating expense in the profit and loss statement.

Expense Method

LEDGER ACCOUNTS

OFFICE SUPPLIES (An expense account)

Mar. 1	*125*	200	Dec. 31	75

UNUSED OFFICE SUPPLIES (An asset account)

Dec. 31	75		

ACCOUNTS PAYABLE

		Mar. 1	200

The balance of the account with Office Supplies amounting to $125 should be listed as an operating expense in the profit and loss statement, while the balance of the account with Unused Office Supplies amounting to $75 should be listed as a current asset in the balance sheet.

XXXII FIXED ASSETS AND DEPRECIATION

Property acquired for use in the operation of a trade or a business may consist of personal property, such as office equipment, store equipment, and delivery equipment, or of real property, such as land and buildings. Such property constitutes the fixed assets of an enterprise. Fixed assets are sometimes referred to as *capital assets* for the reason that their cost represents a capital expenditure rather than a revenue expenditure.

Some fixed assets are tangible and some are intangible. Equipment, buildings, and land constitute tangible assets, while goodwill, patents, copyrights, trade marks, etc., constitute intangible assets.

Some fixed assets are depreciable, while others are not. Most of the tangible fixed assets are subject to depreciation. Land, however, is not considered a depreciable asset.

Acquisition of Fixed Assets. Fixed assets may be bought for cash or on credit. The value at which fixed assets should be recorded is the total cost when acquired and ready for operation or use. The cost may include the purchase price, transportation charges, installation costs, and any other costs that are incurred up to the point of making the assets available for use. In some cases interest may be included in the cost. For example, if money is borrowed for the purpose of constructing a building or other facilities, it is considered sound accounting to add to the cost of such building or facilities the interest incurred during the period of construction. It is important that the cost of depreciable assets be properly accounted for, because the total cost becomes the basis for the annual depreciation charge.

Transactions involving the purchase of fixed assets may be recorded in the appropriate book of original entry by debiting the proper asset account and by crediting the bank account for the amount paid or by crediting the proper liability account, such as Accounts Payable, Notes Payable, or Mortgages Payable, for the obligations incurred.

Additions or improvements representing an increase in the value of fixed assets should be recorded by debiting the proper asset accounts and by crediting the bank account or the proper liability account. For example, if an addition to a building is constructed, the total cost incurred should be debited to the building account. In the same manner, such improvements as the installation of partitions, shelving, hardwood floors, a sprinkler system, air conditioning, or any other improvements that increase the value of property should be recorded by debiting the proper asset accounts for the cost of the improvements. The cost of landscaping grounds surrounding an office or factory building, constructing new driveways, planting trees and shrubbery, and similar improvements should all be capitalized by debiting the proper asset accounts. Assessments for street improvements, sidewalks, sewers, flood prevention, parks, etc., represent improvements that should be recorded by debiting the proper asset accounts.

Fixed Asset Accounts. The determination of asset account titles depends upon the method of accounting for fixed assets. The grouping or classification of fixed assets varies through all degrees of refinement, from a single composite account to the extreme limit of unit accounting, which requires a separate account for each asset. The following are the most commonly used methods:

(a) A composite account.
(b) Classified accounts.
(c) Group accounts.
(d) Unit accounts.

A Composite Account. Under this method of accounting for fixed assets, all depreciable assets are included in one account. For example, in a manufacturing enterprise all of the depreciable assets used in the manufacturing process may be charged to a single plant account. Thus the plant account may be charged with the cost of buildings, machinery, fixtures, and all other equipment used in manufacturing.

Classified Accounts. Under this method of accounting for fixed assets, all depreciable assets are classified into groups where use is the guiding factor. This is a modification of the composite method of accounting for fixed assets. The most generally used classifications are the following:

(a) Buildings.
(b) Machinery and equipment.
(c) Office furniture and fixtures.
(d) Transportation equipment.

Group Accounts. Under this method of accounting for fixed assets, all depreciable assets that are similar in kind and that have approximately the same average useful lives are charged to one account. This method differs from the composite account and the classified accounts methods in that only assets that have approximately the same average useful lives are charged to one account. The greater the number of items that, because of life characteristics, fall in the same group, the more accurate are the results. Under the group method of accounting, fixed assets might be classified as follows:

(a) Office machines.
(b) Office furniture.
(c) Store fixtures.
(d) Delivery trucks.
(e) Portable office partitions.
(f) Air conditioning equipment.
(g) Lighting equipment.

Unit Accounts. Under this method of accounting for fixed assets, a separate account is kept for each individual item constituting a depreciable fixed asset. Thus the following separate accounts might be kept for the fixed assets maintained in one office:

(a) Manager's office desk.
(b) Manager's office chair.
(c) Secretary's desk.
(d) Secretary's chair.
(e) Typewriter.
(f) Bookcase.
(g) Filing cabinet.

Fixed Asset Records. Regardless of the method used in accounting for depreciable assets, it is advisable to keep a detailed record of each item individually. The record may be in bound or loose-leaf book form or in card form. It is important that the proper detailed information be recorded. In determining what information should be recorded, it is advisable to take into consideration the income tax regulations governing depreciation allowances. Since depreciation of fixed assets is an allowable deduction in computing net income for income tax purposes, it is of great importance that such records be kept as will enable the taxpayer to ascertain the amount of depreciation sustained during each accounting period.

The taxpayer must be prepared to prove the reasonableness of the amount of depreciation claimed as a deduction in computing net income. If a proper record is kept of each depreciable asset, no difficulty should be experienced in preparing the schedules that are necessary to establish the taxpayer's right to deduct a reasonable amount of depreciation. In preparing an income tax return the taxpayer must fill in a schedule supplying the following information with respect to property on which depreciation is claimed:

(a) Kind of property.
(b) Date acquired.
(c) Cost.
(d) Assets fully depreciated in use at end of year.
(e) Depreciation allowed (or allowable) in prior years.
(f) Remaining cost to be recovered.
(g) Estimated life used in accumulating depreciation.
(h) Estimated remaining life from beginning of year.
(i) Depreciation allowable this year.

FIXED ASSET RECORD

Description Typewriter Account Office Equipment

Age when acquired New Estimated life 4 years Estimated salvage value $30 Rate of annual depreciation 20%

COST

Date Purchased		Description	Amount
1949			
Jan.	7	Underwood Typewriter	150 00
		#6200625	
		Office Supply Co.	
		City	

DEPRECIATION RECORD

Year	Rate	Amount	Total to date
1949	20%	30 00	30 00
1950	20%	30 00	60 00
1951	20%	15 00	75 00
19			
19			
19			
19			
19			
19			
19			
19			
19			
19			
19			
19			
19			

SOLD, EXCHANGED, OR DISCARDED

Date		Explanation	Amount Realized	More than Book Value	Less than Book Value	Debit Reserve
1951						
July	1	Sold	80 00			75 00

Illustration No. 53, Fixed Asset Record

While it is important to keep a detailed record of fixed assets for income tax purposes, it is also vitally important to keep detailed property records for insurance purposes and as an aid to sound business management. A model filled-in card record of a depreciable asset is reproduced in Illustration No. 53. This provides a detailed record of a typewriter from the time it was purchased to the time it was sold. Following is a narrative of the transactions that were recorded on the card:

January 7, 1949. Purchased Underwood Typewriter, No. 6200625, from the Office Supply Co., City, for $150.

December 31, 1949. Depreciation of typewriter at annual rate of 20 per cent, $30.

December 31, 1950. Depreciation of typewriter at annual rate of 20 per cent, $30.

July 1, 1951. Sold typewriter for $80 cash.

Before the sale of the typewriter on July 1, 1951 was recorded, the depreciation sustained for the half year, amounting to $15, was recorded by debiting Depreciation of Office Equipment and by crediting Reserve for Depreciation of Office Equipment. The amount of this depreciation was also entered on the record card. The sale was then recorded as indicated by the following general journal entry:

Bank	$80.00	
Reserve for Depreciation of Office Equipment	75.00	
Office Equipment		$150.00
Gain on Sale of Office Equipment		5.00
Sold typewriter.		

The sale was also entered on the record card, after which the card was transferred from a file of assets owned to a file of assets sold, exchanged, or discarded. Such an asset record, when properly kept, will provide all the information needed in claiming the proper amount of depreciation of fixed assets as a deduction from gross income in the annual income tax returns. The gain resulting from the sale of the typewriter for $5 more than its book value represents taxable income, which must be reported in the income tax return for the year in which the sale was made.

Depreciation. Depreciation is an expense arising from the exhaustion, or wear and tear of property used in a trade or business, including a reasonable allowance for *obsolescence.* Obsolescence results from progress of the arts and sciences, changed economic conditions, legislation, or other factors that ultimately result in the retirement or other disposition of property. The amount of the decrease in the value of a depreciable asset cannot be determined exactly until the asset has been sold, exchanged, or discarded. It is therefore necessary to estimate the amount of depreciation sustained currently in order that each accounting period may be charged with its proportionate share of such depreciation. It is customary to establish the annual rate of depreciation applicable to each depreciable asset at the time it is acquired. In establishing rates of depreciation of fixed assets, the following factors need to be taken into consideration:

(a) Cost.
(b) Estimated useful life.
(c) Estimated scrap or salvage value at end of useful life.

When the unit method of accounting for depreciable assets is used, it is a simple matter to compute the annual rate of depreciation on each asset after determining (a) its cost, (b) its estimated useful life, and (c) its estimated scrap or salvage value. Suppose, for example, that a machine is purchased for $1,000. Its useful life is estimated to be ten years. At the end of the ten-year period, it is estimated that it will have a salvage value of $100. Under these conditions it is necessary to provide for a total depreciation of $900 over a period of ten years, or $90 a year, which is equivalent to a rate of 9 per cent a year.

When the composite or classified method of accounting for depreciable assets is used, an overall composite rate is applied to the total cost of the assets in computing the depreciation. The rate is determined by applying the appropriate component rate to the cost of each classification or group included in the composite account and by dividing the total amount thus obtained by the total cost of all depreciable property.

Suppose, for example, that the assets charged to a plant account consist of the following groups:

Building	$100,000
Machinery	25,000
Tools	5,000
Other Equipment	10,000
Total Cost	$140,000

The estimated annual rate of depreciation applicable to each group is as follows:

Building	2%
Machinery	10%
Tools	50%
Other Equipment	10%

In computing the rates of depreciation applicable to each group, the usual factors, including (a) cost, (b) estimated useful life, and (c) estimated scrap or salvage value, were taken into consideration. By applying the component rate to the cost of each group of assets, the total depreciation is ascertained as follows:

Building	$100,000	@ 2%	=	$2,000
Machinery	25,000	@ 10%	=	2,500
Tools	5,000	@ 50%	=	2,500
Other Equipment	10,000	@ 10%	=	1,000
Totals	$140,000			$8,000

$8,000 ÷ $140,000 = 5 5/7% Composite rate of depreciation

After determining the composite rate of depreciation applicable to the plant account, it is only necessary to apply this rate to the total cost of the assets included in the plant account in computing the amount of depreciation sustained on the plant each year. It is necessary to redetermine the composite rate whenever substantial changes occur in the relative proportions of different groups of assets included in the composite account.

When the group method of accounting for depreciable assets is used, the computation of the group rate is relatively simple because all of the assets in the group should have approximately the same average useful life. Therefore, the rate applicable to the group is the same as the rate applicable to each asset included in the group. Thus, if an account with office equipment is maintained and each asset charged to that account has an estimated useful life of ten years with no scrap or salvage value, the average annual rate of depreciation would be 10 per cent.

The estimated life of depreciable assets is usually determined from the experience of the enterprise or from data obtained from other sources, such as trade associations. It is obvious that there may be considerable variation in the estimated useful life of different assets used in different enterprises under different conditions. There are no arbitrary methods of estimating the useful life of depreciable assets, but statistics based on experience serve as a reliable guide in estimating the useful life of the depreciable assets of any trade or business.

In this discussion the *straight-line* or fixed-percentage method of computing depreciation is implied. This method assumes that the rate of depreciation will be uniform during the useful life of the property. While other methods of computing depreciation may be used, the income tax regulations prescribe that any method used must be reasonable and must have due regard to operating conditions during the taxable period. The simplicity of the straight-line method of determining depreciation has made it the most popular method, and it appears to be as accurate as any other so-called scientific method of computing depreciation.

Recording Depreciation. After the total amount of depreciation applicable to an accounting period is computed, it should be recorded by debiting the proper expense accounts and by crediting either the proper asset account or the proper reserve account. If the depreciation is credited to the asset accounts, it is known as the "direct method of recording depreciation." If the depreciation is credited to a reserve account, it is known as the "reserve method of recording depreciation." While both methods are approved by the Treasury Department for income tax purposes, accountants generally prefer the reserve method.

When the direct method of recording depreciation is used, the balance of each fixed asset account represents the book value of the asset. When the reserve method of recording depreciation is used, it is necessary to take into consideration both the asset accounts and the reserve accounts in determining the book value of the fixed assets. Thus, if an account with Office Equipment is maintained and it has a debit balance of $10,000 and a reserve for depreciation of office equipment account has a credit balance of $2,500, the book value of the office equipment is the difference between the debit balance of the office equipment account and the credit balance of the reserve account, or $7,500.

Depreciation Expense Accounts. One or more expense accounts may be used in recording depreciation. The total depreciation sustained during an accounting period may be debited to one account with depreciation expense, or the depreciation of each asset or each group of assets may be charged to a separate expense account. Thus, if separate accounts are kept with office equipment, store equipment, and delivery equipment, separate expense accounts may also be kept for the depreciation of each of these types of equipment. Recording the depreciation of each type of equipment in a separate account facilitates a proper classification of depreciation expense in the profit and loss statement. If a single account with depreciation expense is kept, it may be necessary to analyze the account at the close of each accounting period before the profit and loss statement is prepared in order that depreciation expense may be classified on the desired basis. For example, it may be desired to classify the depreciation of office equipment as an administrative expense and the depreciation of delivery equipment as a selling expense.

Depreciation Reserve Accounts. One or more reserve accounts may be used in recording depreciation. The total depreciation sustained during an accounting period may be credited to one reserve account, or the depreciation of each asset or of a group of assets may be credited to a separate reserve account. Thus, if separate accounts are kept with office equipment, store equipment, and delivery equipment, separate reserve accounts may also be kept for the depreciation of each of these types of equipment. Recording the depreciation of each type of equipment in a separate reserve account makes it possible to list the amount of the reserve applicable to each equipment account as a deduction from the cost of the equipment in the balance sheet. For example, if the office equipment account has a debit balance of $10,000 and the reserve for depreciation of office equipment account has a credit balance of $2,500, the accounts may be listed in the balance sheet under the heading of fixed assets as follows:

Office Equipment	$10,000.00	
Less Reserve for Depreciation	2,500.00	$7,500.00

Bryant & Wood use the group method of accounting for depreciable assets and keep the following accounts incident thereto:

Fixed Assets

21 Store Equipment

021 Reserve for Depreciation of Store Equipment

22 Delivery Equipment

022 Reserve for Depreciation of Delivery Equipment

23 Office Equipment

023 Reserve for Depreciation of Office Equipment

Selling Expenses

725 Depreciation of Store Equipment

726 Depreciation of Delivery Equipment

Administrative Expenses

741 Depreciation of Office Equipment

It will be observed that separate accounts are kept for recording (a) the cost of fixed assets, (b) the depreciation of fixed assets, and (c) the reserve for depreciation of each group of depreciable assets. A card record of each depreciable asset is also kept by Bryant & Wood in order that the detailed information needed in preparing income tax returns will be available.

In addition to depreciation expenses, other expenses, such as repairs, insurance, and taxes, may be incurred in connection with the ownership of fixed assets. Separate accounts should be maintained for recording each of these expenses. Sometimes separate accounts are kept for recording the expenses incurred in connection with each kind of equipment. For example, separate accounts for repairs, insurance, and taxes applicable to delivery equipment are kept if it is desirable to determine the total cost of delivering goods. It should be understood that a separate account may be kept for recording any expense that may be incurred in the operation of a business enterprise.

Disposition of Fixed Assets. A fixed asset may be disposed of in any one of the following ways:

(a) It may be discarded or retired.
(b) It may be sold.
(c) It may be exchanged or traded in for property of like kind or for other property.

Discarding or Retiring Fixed Assets. A fixed asset may be discarded or retired whether or not it has been fully depreciated. If it has been fully depreciated, no gain or loss will be sustained. If it has not been fully depreciated, the book value of the discarded asset will represent a loss. Such a loss may be the result of underestimating the depreciation of the asset for the period of time that it has been in use, or it may be the result of obsolescence. Often it is better to scrap an obsolete machine and to buy a new one even though a loss is sustained on the old machine.

On July 16, Bryant & Wood discarded parcel-post scales that had no exchange or sale value. The fixed asset record indicated that the scales originally cost $80 and that depreciation amounting to a total of $60 had been recorded as a credit to an account with reserve for depreciation of store equipment.

This transaction involved a loss of $20 resulting from the discard of the asset, which had a book value of $20. The transaction should be recorded as indicated by the following general journal entry:

Loss on Discarded Store Equipment................	$20.00	
Reserve for Depreciation of Store Equipment........	60.00	
Store Equipment................................		$80.00
Discarded parcel-post scales.		

When this entry is posted, the debit of $60 to the reserve account and the credit of $80 to the store equipment account will have the effect of eliminating the parcel-post scales from the balances of these accounts. The debit of $20 to Loss on Discarded Store Equipment has the effect of setting up the loss sustained.

When a fixed asset is discarded after it has been fully depreciated, no loss will result from the transaction, but the discarded asset should be eliminated from the account balances by debiting the reserve account and by crediting the asset account for an amount equal to the original cost of the asset. In no case will gain result from discarding or retiring a fixed asset.

Selling Fixed Assets. If a fixed asset is sold, it is necessary to know its book value before the proper amount of any profit or loss resulting from the transaction can be determined. The book value of an asset is the difference between its cost and the amount of depreciation recorded. Thus, if a typewriter that cost $150 depreciates at the rate of 20 per cent a year and the annual depreciation is recorded by debiting Depreciation of Office Equipment and by crediting Reserve for Depreciation of Office Equipment, the book value of the typewriter at the end of three years will be the difference between the cost price of the typewriter and the credit balance of the reserve account, or $60. In other words, the book value of an asset is the net value recorded in the books. When a fixed asset is sold at its book value, no profit or loss results from the transaction; when it is sold for more than its book value, the difference represents a gain; when it is sold for less than its book value, the difference represents

Assuming that the typewriter was sold at the end of three years for $65 cash, the transaction should be recorded as indicated by the following general journal entry:

Bank	$65.00	
Reserve for Depreciation of Office Equipment	90.00	
Office Equipment		$150.00
Gain on Sale of Office Equipment		5.00

Sold typewriter.

When this entry is posted, the debit of $90 to the reserve account will offset the amount recorded previously as a credit to the reserve because of the estimated depreciation of the typewriter over a period of three years. The amount credited to Office Equipment will offset the purchase price previously recorded as a debit to Office Equipment. These entries have the effect of completely eliminating the value of the old typewriter from the office equipment and reserve accounts. The gain realized from the sale of the typewriter for $5 more than its book value is recorded as a gain on sale of office equipment. This gain should be listed under the heading of "Other Income" in the profit and loss statement and must be included in gross income in the income tax return.

If the typewriter referred to on the preceding page was sold at the end of three years for $55 instead of $65, there would be a loss of $5 instead of a gain of $5. The transaction should be recorded as indicated by the following general journal entry:

Bank	$55.00	
Reserve for Depreciation of Office Equipment	90.00	
Loss on Sale of Office Equipment	5.00	
Office Equipment		$150.00

Sold typewriter.

When this entry is posted, the debit of $90 to the reserve account and the credit of $150 to the office equipment account will eliminate the value of the old typewriter from the account balances. The loss resulting from the sale of the old typewriter for $5 less than its book value will be recorded as a loss on sale of office equipment. This loss should be listed under the heading of "Other Charges" in the profit and loss statement and may be claimed as a deduction from gross income in the income tax return.

Exchange of Fixed Assets. A fixed asset may be exchanged or traded in for property of like kind or for other property. The *exchange allowance* may be equal to the book value of the property exchanged or it may be more or less than the book value. The federal income tax law should be taken into consideration in recording transactions involving exchanges of property held for productive use in trade or business or held for investment. The following is quoted from the income tax regulations:

"No gain or loss is recognized if (1) a taxpayer exchanges property held for productive use in his trade or business, together with cash, for other property of like kind for the same use, such as a truck for a new truck or a passenger automobile for a new passenger automobile to be used for a like purpose, or (2) a taxpayer who is not a dealer in real estate exchanges city real estate for a ranch or farm, or improved real estate for unimproved real estate, or (3) a taxpayer exchanges investment property and cash for investment property of a like kind."

To avoid confusion in preparing income tax returns and to eliminate the need for making adjustments in computing the taxable income, it is generally deemed advisable to record transactions involving exchanges of property in such a manner as to conform to the income tax regulations.

Regardless of the amount of the allowance received for old property exchanged for new property of like kind, the new property acquired should be recorded at cost. To find the cost, it is necessary to take into consideration (a) the book value of the old property given in exchange plus (b) the amount paid in cash or to be paid in cash.

A delivery truck costing $1,400 was charged to a delivery equipment account and depreciation amounting to $420 was credited to a reserve account each year for three years. The book value of the truck after three years was $140, as shown by the following computation:

Cost of truck	$1,400.00
Less amount reserved for depreciation	1,260.00
Book value	$ 140.00

If this truck is traded in on a new truck to be used for a similar purpose and $1,200 is paid in cash, the cost of the new truck is $1,340 ($1,200 + $140). This transaction should be recorded as indicated in the following general journal entry:

Delivery Equipment (new truck)	$1,340.00	
Reserve for Depreciation of Delivery Equipment	1,260.00	
Delivery Equipment (old truck)		$1,400.00
Bank		1,200.00
Purchased a new truck.		

When this journal entry is posted, the cost of the old truck will be eliminated from the delivery equipment account and that account will be charged for the cost of the new truck, which constitutes the basis for future depreciation charges. The amount reserved for depreciation of the old truck will also be eliminated from the reserve account. It will be seen that no gain or loss was recognized in recording the transaction; hence the method of accounting conforms to the income tax regulations.

Some accountants prefer to take into consideration the amount of the exchange allowance rather than the book value of an asset given in exchange in determining the cost of the new asset acquired. However, if this practice is followed, it will be necessary to adjust the accounts in preparing the annual income tax return. These adjustments can become quite complicated where there are frequent transactions involving the exchange of fixed assets. It is, therefore, generally preferable from a practical standpoint to follow the income tax regulations in recording such transactions so that no adjustments will be necessary in preparing the income tax returns.

In any transaction involving an exchange in which property is exchanged for property not of like kind, any gain or loss resulting from the transaction should be recorded, since it must be taken into consideration in preparing the income tax return. Any gain resulting from such an exchange is taxable and must be reported; any loss sustained should be claimed as a deduction.

A typewriter costing $150 was charged to an office equipment account and depreciation on the typewriter amounting to $30 was credited to a reserve account each year for two years. At the end of two years the typewriter was traded in on a new cash register costing $400. The trade-in allowance amounted to $115, the balance being paid in cash. Since this transaction did not involve an exchange of property for other property of like kind, any gain realized or loss sustained will be recognized for income tax purposes; hence it should be recorded in the same manner as it would be if the typewriter had been sold for $115 and the proceeds applied on the purchase of the new cash register. The transaction should therefore be recorded as indicated in the following general journal entry:

Store Equipment	$400.00	
Reserve for Depreciation of Office Equipment	60.00	
Office Equipment		$150.00
Bank		285.00
Gain on Sale of Office Equipment		25.00
Purchased a new cash register.		

When this entry is posted, the debit of $60 to the reserve account will offset the amount recorded previously as a credit to the reserve because of the estimated depreciation of the typewriter over a period of two years. The amount credited to Office Equipment will offset the purchase price of the typewriter previously recorded as a debit to Office

Equipment. These entries have the effect of completely eliminating the value of the old typewriter from the office equipment and reserve accounts. The gain realized on the old typewriter is recorded as a gain on sale of office equipment. Had the trade-in allowance been less than the book value of the typewriter, the difference would represent a loss that should be charged to Loss on Sale of Office Equipment.

Real Estate. Property consisting of land and permanent improvements thereon is known as real estate. Real estate may be acquired for investment purposes; it may also be acquired for business use or as the home of a business.

The method of accounting for real estate is the same regardless of whether it is acquired as investment property for income purposes or as business property to be used as a home for the business. It is advisable to keep separate accounts for the land and the buildings because the buildings only are subject to depreciation and the depreciation of the buildings used by a business constitutes a business expense.

The method of computing and of recording the depreciation on buildings is the same as for other fixed assets. To illustrate, it will be assumed that on January 2, Moore & Son paid $100,000 in cash for real estate to be used as a home for the business. Of the purchase price, $30,000 was allocated to the land and $70,000 to the building. This transaction was recorded as indicated by the following general journal entry:

Land	$30,000.00	
Building	70,000.00	
Bank		$100,000.00
Purchased real estate.		

It was estimated that the building would have a useful life of 40 years with a salvage value of $5,600 at the end of that period; hence the rate of depreciation was ascertained in the following manner:

Cost of building	$70,000.00
Salvage value	5,600.00
Total depreciation	$64,400.00

$64,400 ÷ 40 years = $1,610 annual depreciation

$1,610 ÷ $70,000 = 2.3% rate of depreciation

The annual depreciation of the building was recorded as indicated in the following general journal entry:

Depreciation of Building	$1,610.00	
Reserve for Depreciation of Building		$1,610.00
Annual depreciation.		

When real estate is sold, the transaction should be recorded in the same manner as transactions arising from the sale of other fixed assets. The difference between the amount received from the sale and the book value of the property represents gain or loss that should be recognized in recording the transaction. The book value is the difference between the cost of the property and the amount reserved for depreciation of the property.

Assume that the real estate purchased by Moore & Son on January 2 was sold ten years later for $90,000 cash, $35,000 being allotted to the land and $55,000 being allotted to the building. Before the sale can be recorded in the books of Moore & Son, it is necessary to ascertain the book value of the property sold. Since the land was recorded at a cost of $30,000 and it is not subject to depreciation, the book value at the time of the sale is the same as its original cost. The building was recorded at its cost of $70,000; the annual depreciation at the rate of 2.3 per cent, amounting to $1,610, was credited to a reserve account. At the end of ten years the book value of the building was the difference between its cost and the total amount credited to the reserve, or $53,900. With this information the transaction may be recorded as indicated in the following general journal entry:

Bank	$90,000.00	
Reserve for Depreciation of Building	16,100.00	
Land		$30,000.00
Building		70,000.00
Gain on Sale of Land		5,000.00
Gain on Sale of Building		1,100.00
Sold real estate.		

When a depreciable asset is sold, any depreciation sustained prior to the date of the sale and not previously recorded should be recorded before the sale is recorded. It is necessary to record such depreciation before the book value at time of sale can be determined, and the book value must be determined before any gain or loss resulting from the sale can be ascertained.

Fully Depreciated Fixed Assets. A fixed asset is said to be fully depreciated when the recorded depreciation is equal to the cost of the asset less its scrap or salvage value, if any. When an asset is fully depreciated, no further depreciation should be recorded. Since the rate of depreciation is based on its estimated useful life, an asset may be continued in use after it is fully depreciated. In this case, the cost of the asset and the amount reserved for depreciation are usually retained in the accounts, although some accountants prefer to adjust the accounts when a fixed asset has been fully depreciated so as to remove the cost value of the asset and the amount reserved for depreciation thereon from the accounts. This adjustment should be made when a fully depreciated asset is scrapped. The adjustment involves a debit to the proper reserve account and a credit to the proper fixed asset account for the cost value of the asset.

In some states a taxable value is placed on a fully depreciated fixed asset if the asset is continued in use. Under such circumstances, the taxable value of the fully depreciated asset should be stated in the fixed asset record as a guide in preparing the property tax schedule. The taxable values of fully depreciated fixed assets and the book value of other fixed assets should be listed so that the total taxable value of the fixed assets may be ascertained.

It should be observed that there is a similarity in accounting for supplies and prepaid items and for fixed assets when the asset method of accounting is used. Under this method, purchases of supplies and services that may not be consumed in the same accounting period are recorded as assets. At the end of the period the portion consumed is then charged to the proper expense accounts and is credited to the proper asset accounts. In the case of fixed assets, purchases are charged to asset accounts and periodically the decrease in value resulting from depreciation is charged to the proper expense accounts and is credited to the proper reserve accounts. It will be seen that in both cases transactions arising from purchases involve debits to asset accounts and credits to either Accounts Payable or the bank account. Also in both cases adjusting entries are made periodically to record the expenses arising from the exhaustion, consumption, or use of the assets.

PRACTICE ASSIGNMENT No. 32. Complete Report No. 32 in the workbook and submit your working papers to the instructor for approval. Then continue with the next study assignment in Unit Sixteen until Report No. 33 is required.

Unit Sixteen

ACCOUNTING FOR TAXES

XXXIII SOCIAL SECURITY TAXES

The payroll taxes imposed for social security purposes are divided into two classes as follows:

(a) Taxes imposed for old-age and survivors' insurance benefits and for other welfare purposes.

(b) Taxes imposed for unemployment compensation purposes.

The taxes imposed for old-age and survivors' insurance benefits and for other welfare purposes apply to both employers and employees. That portion of the tax which is imposed on employees must be withheld by employers from the wages paid to their employees. That portion of the tax which is imposed on employers represents a business expense that should be treated as one of the operating expenses of a business.

Taxes imposed for general revenue purposes include income taxes, sales taxes, and property taxes. These taxes differ from payroll taxes in that they are imposed as a means of raising the revenue needed by federal, state, and local governments out of which the operating expenses of the government may be paid. Since March 1, 1913, the Federal Government has derived a large portion of its revenue from income taxes. Many of the states also impose a tax on income. In recent years most of the states have enacted laws imposing a tax on sales. Sales taxes provide a large portion of the current revenue needed by the states in meeting their operating expenses. Property taxes have long been the principal source of revenue from which the local subdivisions of government meet their operating expenses.

Experience in administering relief to dependent, aged, and unemployed persons during the depression years following 1929 resulted in the enactment of a series of social security laws intended to alleviate the principal causes of economic insecurity. Under these laws taxes are imposed on both employers and employees for the purpose of providing funds from which old-age and survivors' insurance benefits and unemployment compensation benefits may be paid. Old-age and survivors' insurance benefits are paid out of federal funds, while unemployment compensation benefits are paid out of state funds. These funds are created by taxes imposed on wages.

Employer and Employees. Any individual engaged in business as a sole proprietor or as a partner, or any corporation, employing one or more individuals for the performance of services within the United States, is an employer. In a sole proprietorship the owner or proprietor is not considered an employee. He is an employer, however, if he employs one or more persons. In a partnership the partners are not considered employees. The partnership is an employer, however, if it employs one or more persons in a covered employment.

In a corporation the officers are considered employees. The officers may include a president, one or more vice-presidents, a secretary, a treasurer, and other officers. Such officers may be considered employees even though they receive no compensation for the services rendered to the corporation. A director of a corporation, however, is not considered an employee unless he performs services for the corporation other than those required by attendance at and participation in meetings of the board of directors. Where an individual is both an officer and a director of a corporation, he is, of course, considered an employee and must be counted in determining whether or not the corporation is liable for payroll taxes and the amount of remuneration he receives as an officer must be included in computing taxable wages.

Old-Age Insurance Taxes. The following table shows the rates of the taxes imposed under the Federal Insurance Contributions Act (F.I.C.A.) for old-age and survivors' insurance benefits:

	Employment Tax on Wages		Tax on Self-Employment Income
Years	Employers	Employees	
1951–1953	1½%	1½%	2¼%
1954–1959	2%	2%	3%
1960–1964	2½%	2½%	3¾%
1965–1969	3%	3%	4½%
1970 and after	3¼%	3¼%	4⅞%

The tax on wages is imposed on a basis of calendar years, while the tax on self-employment income is imposed on a basis of taxable years. A taxable year may be a calendar year or it may be a fiscal year ending on the last day of any month other than December. A taxable year for the purpose of the tax on self-employment income is the same as the taxpayer's taxable year for federal income tax purposes.

Taxable Wages. The term "wages" means all remuneration received for employment including the cash value of all remuneration paid in any medium other than cash. Prior to January 1, 1951, only the first $3,000 of wages received by each employee during any calendar year were subject to the taxes imposed for old-age and survivors' insurance benefits. Beginning January 1, 1951, the base of the tax was increased to the first $3,600 of wages received by each employee during any calendar year. The amount of wages received by an employee in excess of this limit should be excluded, therefore, in computing the tax.

Self-Employment Income. Beginning January 1, 1951, self-employed workers, other than farmers and certain professional persons, whose annual net income amounts to at least $400 are covered and such workers are subject to the tax imposed for the purpose of old-age and survivors' insurance benefits. The tax is imposed on a basis of their net earnings from self-employment.

Net earnings from self-employment are determined by ascertaining the sum of:

(1) Gross income derived by an individual from any trade or business carried on, less allowable deductions attributable to such trade or business, and

(2) The individual's distributive share (whether or not distributed) of the ordinary net income or loss from any trade or business carried on by a partnership of which he is a member.

Ordinarily the net business income of an individual as shown in his income tax return will constitute his net earnings from self-employment for the purpose of the Social Security Law. Earnings of less than $400 from self-employment are ignored. The maximum self-employment income of any individual for a taxable year is $3,600.

As explained on page 165, the self-employment tax is payable on the fifteenth day of the third month following the close of the taxable year. For self-employed individuals filing their return on the calendar-year basis, the tax is, therefore, not payable until March 15 of the succeeding year. Since the self-employment tax is usually treated as a personal expense of the proprietor, it is not recorded in the books of the business unless the tax is paid out of business funds, in which case the amount paid is charged to the proprietor's drawing account. In the case of partnerships, the self-employment tax, like the income tax, is imposed on the individual partners rather than on the partnership. If, however, the self-employment tax of a partner were paid out of partnership funds, the amount should be charged to the partner's drawing account, just as any other personal expense paid out of partnership funds should be charged to the proper partner's drawing account.

Unemployment Taxes. Under the Federal Unemployment Tax Act, a tax is imposed on employers of eight or more persons. The rate of the federal tax imposed for unemployment purposes is 3 per cent; however, credit not to exceed 90 per cent of the tax imposed under the federal law is allowed for contributions paid into the unemployment funds of the states. All forty-eight states have enacted laws imposing taxes on employers for unemployment compensation purposes. These state laws are not entirely uniform as to coverage. In some states all employers of one or more persons are covered, while in other states employers of less than eight employees are not covered. Certain types of business and employment are also exempted from the tax. While the rates of contribution required under state laws vary considerably, the basic rate in most states is 2.7 per cent. Some states have merit rating systems under which the annual rate of contributions required of each employer is based on his unemployment experience. Even though an employer is granted a lower rate than 2.7 per cent because of a favorable employment record, he may be allowed credit of 90 per cent of the tax imposed under the federal law.

It will be seen that employers may be subject to two distinct taxes for unemployment purposes. The basic federal rate is 3 per cent, while the basic rate in most states is 2.7 per cent of the wages paid. Only the first $3,000 of wages paid to each employee are taxable under the federal law and under the laws of most of the states.

Since the federal tax rate is 3 per cent and employers are permitted to claim credit up to 90 per cent of the federal tax for contributions made to the unemployment compensation funds of the states, the total tax burden for this purpose is usually 3 per cent, divided as follows:

(a) 2.7 per cent of the taxable wages to be paid into the state unemployment compensation fund, and

(b) .3 per cent to be paid to the Federal Government.

From the total amount paid to the Federal Government each year in unemployment taxes, Congress appropriates and allots to each state an amount to take care of the administrative cost of operating the state unemployment plans. Benefits to unemployed workers are paid from the state unemployment compensation funds.

An analysis of the laws of all the states indicates that, to be eligible to receive unemployment compensation benefits, an individual must meet the following requirements:

(a) He must have been employed for a certain length of time within a specified period in an employment covered by the law.
(b) He must have served the required waiting period.
(c) He must be available for work and be registered at a state employment office.
(d) He must be capable of working.
(e) He must not have refused employment for which he is reasonably fitted.
(f) He must not be out of work because of a strike or lock-out still in progress.
(g) He must not be self-employed.

A few states require contributions for unemployment purposes from employees as well as from employers. Employers located in such states are required to withhold the amount of the contributions required of employees from their wages in the same manner as federal old-age insurance taxes are withheld.

An employer may be subject to social security taxes imposed by either the Federal Government or the state governments, or by both. He may be subject to the social security taxes imposed either for old-age and survivors' insurance or for unemployment purposes, or for both. All employers of one or more persons, not specifically exempted, are subject to the tax imposed for old-age and survivors' insurance purposes. All employers of eight or more persons, not specifically exempted, are subject to the tax imposed under the Federal Unemployment Tax Act. Such employers may also be required to make contributions to the state unemployment compensation funds.

Recording Federal Old-Age Insurance Taxes. Employers who are subject to the tax imposed for old-age and survivors' insurance purposes only, need keep but two accounts to record such taxes as follows:

(a) Social Security Taxes — an expense account.

(b) Social Security Taxes Payable — a liability account.

Such taxes as the employer is required to withhold from the employees' wages for this purpose may be recorded by crediting Social Security Taxes Payable. At the time wages are paid, it is necessary to debit Wages for the total amount of wages earned, to credit Social Security Taxes Payable for the amount withheld, and to credit the bank for the difference. Thus, if the total taxable wages for a given pay period amounted to $400 and the tax withheld by the employer amounted to $6, the transaction may be recorded as indicated in the following general journal entry:

Wages	$400.00	
Social Security Taxes Payable		$ 6.00
Bank		394.00
Paid wages due less amount withheld for social security taxes imposed on employees.		

In addition to recording the taxes that the employer is required to withhold from his employees' wages, the tax imposed on the employer should also be recorded. The tax imposed on the employer for this purpose amounts to the same as the tax imposed on his employees. Hence, if the taxable wages earned by employees during a given pay period amounted to $400 and the employer was required to withhold $6, he would also be liable for an additional tax of $6 which may be recorded as indicated in the following general journal entry:

Social Security Taxes	$6.00	
Social Security Taxes Payable		$6.00
Social security tax imposed on employer for old-age insurance purposes.		

It will be seen that, on each payday, entries should be made to record the following social security taxes:

(a) The tax on employees. The employer is required to collect this tax by deducting the amount of the tax from the wages paid.

(b) The tax imposed on the employer.

Both of these taxes are imposed for old-age and survivors' insurance purposes. The tax imposed on the employees represents a liability of the employer but does not constitute an expense of the employer since he withholds the amount of the tax from the employees' wages. The tax imposed on the employer represents both an expense and a liability of the employer.

After the foregoing journal entries have been posted, the social security taxes account will have a debit balance of $6 and the social security taxes payable account will have a credit balance of $12.

The amount credited to Social Security Taxes Payable is a liability of the employer until such time as the amount withheld is paid to the proper government agency. When payment is made, it is necessary only to debit Social Security Taxes Payable and to credit the bank. Thus, if an employer's taxable payroll amounts to $400 a month for three months and a $1\frac{1}{2}$ per cent tax is imposed on both the employees and the employer, at the end of three months the social security taxes payable account will have a credit balance of \$36. When this amount is paid, the transaction may be recorded as indicated by the following general journal entry:

Social Security Taxes Payable	\$36.00	
Bank		\$36.00
Paid social security taxes for quarter.		

At the close of any accounting period, the credit balance of the social security taxes payable account represents the amount of the employer's liability on account of the taxes imposed under the Federal Insurance Contributions Act.

Instead of recording the tax imposed on employers for old-age and survivors' insurance purposes each time wages are paid, some employers record the tax only at the end of each calendar quarter. Since the employer becomes liable for the tax at the time wages are paid, it is better accounting practice to record both the tax on employees and the tax on the employer at the time of recording the payment of wages.

Recording Federal Old-Age Insurance and Unemployment Taxes. While the taxes imposed under the Federal Social Security Law for both old-age and survivors' insurance and for unemployment purposes may be recorded in a single liability account, many accountants prefer to keep separate liability accounts for each type of tax. In such case the following accounts may be kept to record the taxes:

(a) Social Security Taxes — an expense account.
(b) Federal Old-Age Insurance Taxes Payable — a liability account.
(c) Federal Unemployment Taxes Payable — a liability account.

Under this plan the employer's liability for old-age and survivors' insurance taxes payable is recorded in one account, while his liability for the taxes imposed for unemployment purposes is recorded in a separate account.

Even though the employer may be subject to both taxes, it is satisfactory to keep a single expense account in which to record such taxes. However, separate expense accounts may be kept if desired.

To illustrate the recording of such taxes, it is assumed that an employer is subject to the taxes imposed under the Federal Social Security Law for both old-age and survivors' insurance and unemployment purposes. Both the employer and his employees are subject to an old-age and survivors' insurance tax of $1\frac{1}{2}$ per cent, the employer being required to withhold the employees' portion of the tax from the wages paid. The employer is also subject to a 3 per cent tax imposed for unemployment purposes. The total wages earned during a given pay period amounted to $1,200 and the tax withheld from the employees' wages amounted to $18. This transaction may be recorded as indicated by the following general journal entry:

Wages	$1,200.00	
Social Security Taxes	54.00	
Federal Old-Age Insurance Taxes Payable		$ 36.00
Federal Unemployment Taxes Payable		36.00
Bank		1,182.00
Recording wages paid and federal social security taxes payable.		

Analysis of the foregoing transaction:

(a) The amount charged to Wages, $1,200, represents the employees' earnings for the pay period. The result was an increase in the operating expenses of the employer.

(b) The amount charged to Social Security Taxes was computed as follows:

Employer's federal old-age insurance tax, 1½% of $1,200	$18.00
Employer's federal unemployment tax, 3% of $1,200	36.00
Total	$54.00

The result was an increase in the operating expenses of the employer.

(c) The amount credited to Federal Old-Age Insurance Taxes Payable was computed as follows:

Deducted from employees' wages, 1½% of $1,200	$18.00
Employer's tax for federal old-age insurance purposes, 1½% of $1,200	18.00
Total	$36.00

The result was an increase in a liability of the employer.

(d) The amount credited to Federal Unemployment Taxes Payable was computed as follows:

3% of $1,200 = $36, amount of employer's tax for federal unemployment purposes.

The result was an increase in a liability of the employer.

(e) The amount credited to the bank was computed as follows:

Wages earned by employees	$1,200.00
Employees' tax withheld, 1½%	18.00
Net amount of wages paid to employees	$1,182.00

The result was a decrease in an asset of the employer.

When either of these taxes is paid, it is necessary only to debit the proper liability account and to credit the bank. Thus, when the federal old-age and survivors' insurance tax is paid, it is necessary to debit Federal Old-Age Insurance Taxes Payable and to credit the bank. Likewise, when the federal unemployment taxes are paid, it is necessary to debit Federal Unemployment Taxes Payable and to credit the bank.

Recording State Unemployment Contributions. When an employer is required by state law to make contributions to a state unemployment compensation fund, additional accounts may be kept therefor as follows:

(a) State Unemployment Contributions — an expense account.

(b) State Unemployment Contributions Payable — a liability account.

When an employer is required to make contributions to the state unemployment compensation funds of more than one state, it may be found advisable to keep a separate account for the contributions payable to each state. Some employers are required to make contributions to the unemployment compensation funds of all forty-eight states, the District of Columbia, and the territories of Alaska and Hawaii. Thus, it is possible for an employer to be liable for the following social security taxes:

(a) The federal old-age and survivors' insurance tax, including both the tax on the employer and the tax on employees;

(b) The federal unemployment tax; and

(c) The taxes imposed for unemployment compensation purposes by forty-eight states, the District of Columbia, and two territories — a total of fifty-three different social security taxes.

It can readily be seen that accounting for such taxes may become somewhat complicated. For most employers, however, the accounting procedure is simple. Most employers are subject to the federal social security taxes and to the unemployment compensation taxes levied by one state only, that is, the state in which the employer has his place of business. Relatively few employers have employees earning their wages in states other than the one in which their places of business are located.

To illustrate the recording of state unemployment contributions, it is assumed that an employer is required to make contributions to the unemployment compensation fund of one state only and that the tax imposed amounts to 2.7 per cent of the taxable wages earned by his employees. During a given pay period the taxable wages earned amounted to a total of $900. This transaction may be recorded as indicated by the following general journal entry:

Wages	$900.00	
State Unemployment Contributions	24.30	
State Unemployment Contributions Payable		$ 24.30
Bank		900.00
Recording wages paid and state unemployment contributions payable.		

This method of recording state unemployment contributions may be referred to as the accrual method. Both the expense and the liability are recorded at the time the wages are paid, even though the employer is not required to pay the contributions into the state unemployment compensation fund until after the end of the calendar quarter. When the books are kept on the accrual basis, it is advisable to record the liability for unemployment contributions at the time the wages are recorded.

An employer may be subject both to the tax imposed for unemployment purposes under the Federal Social Security Law and to the tax imposed under the unemployment compensation laws of one or more states. In such cases, in computing the amount of the federal tax the employer is permitted to claim credit for state contributions not to exceed 90 per cent of the federal tax. If the federal unemployment tax amounts to 3 per cent and an employer is entitled to the maximum credit for state contributions, the net amount of his federal tax will be only .3 per cent. Under the state unemployment compensation laws, employers generally are required to make contributions to the unemployment funds at a basic rate of 2.7 per cent, which is exactly 90 per cent of the federal tax. In some states due to merit rating, employers may be taxed at reduced rates. However, such a reduction in the tax does not affect the amount of the credit which may be claimed in computing the federal tax. Actually, therefore, the net rate of the federal tax imposed for federal unemployment purposes is usually .3 per cent of the taxable wages.

Under the state unemployment compensation laws employers generally are required to make contributions to the unemployment funds at varying rates depending upon their employment record. The maximum rate usually is 2.7 per cent which is exactly 90 per cent of the federal tax. If an employer is allowed a reduction in the rate of state contributions because of his experience rating he is not penalized in computing the credit allowed under the federal law. Instead, he is allowed additional credit with respect to the amount of the contributions which he is relieved from paying into the state unemployment compensation fund because of a favorable employment record. This is a strong incentive for employers to stabilize employment. By so doing the employer may be required to pay into the state unemployment compensation fund considerably less than 2.7 per cent of his taxable wages and still receive the maximum credit of 90 per cent of the federal tax.

For example: An employer's taxable wages during a certain year amounted to a total of $175,000 all of which was subject to the federal tax imposed on employers by the Federal Social Security Law for unemployment purposes. Assuming that because of a favorable employment record, this employer was required to make contributions to the state unemployment compensation fund of only .7 per cent, the total federal and state taxes imposed for unemployment purposes may be computed as follows:

State unemployment contributions (.7% of $175,000)			$1,225.00
Federal unemployment tax (3% of $175,000)		$5,250.00	
Less credit:			
For state contributions	$1,225.00		
Additional credit	3,500.00	4,725.00	525.00
Total unemployment tax			$1,750.00

The additional credit is computed as follows:

State contributions, had rate been 2.7%	$4,725.00
Contribution at experience rate (.7%)	1,225.00
Difference	$3,500.00

In no case may the credit for state contributions exceed 90 per cent of the federal tax imposed for federal unemployment purposes.

To illustrate the method of recording all social security taxes imposed under both the federal and state laws, it will be assumed that an employer is subject to the following taxes:

(a) Employees' tax imposed for old-age and survivors' insurance purposes — 1½%.
(b) Employer's tax imposed for old-age and survivors' insurance purposes — 1½%.
(c) Federal tax imposed for unemployment purposes — .3%.
(d) State unemployment contributions — 2.7%.

The payroll for a given pay period amounted to $1,400, the entire amount being subject to all social security taxes. This transaction may be recorded as indicated by the following general journal entry:

Wages	$1,400.00	
Social Security Taxes	25.20	
State Unemployment Contributions	37.80	
Federal Old-Age Insurance Taxes Payable		$ 42.00
Federal Unemployment Taxes Payable		4.20
State Unemployment Contributions Payable		37.80
Bank		1,379.00
Recording wages paid and social security taxes payable		

Analysis of the foregoing transaction:

(a) The amount charged to Wages, $1,400, represents the employees' aggregate earnings for the pay period. The result was an increase in the operating expenses of the employer.

(b) The amount charged to Social Security Taxes was computed as follows:

Employer's federal old-age insurance tax, 1½% of $1,400		$21.00
Employer's federal unemployment tax, 3% of $1,400	$42.00	
Less credit for state contributions, 2.7% of $1,400	37.80	4.20
Total		$25.20

The result was an increase in the operating expenses of the employer.

(c) The amount charged to State Unemployment Contributions was computed as follows:

2.7% of $1,400 = $37.80

The result was an increase in the operating expenses of the employer.

(d) The amount credited to Federal Old-Age Insurance Taxes Payable was computed as follows:

Deducted from employees' wages, 1½% of $1,400	$21.00
Employer's tax for federal old-age insurance purposes, 1½% of $1,400	21.00
Total	$42.00

The result was an increase in a liability of the employer.

(e) The amount credited to Federal Unemployment Taxes Payable was computed as follows:

3% of $1,400	$42.00
Less credit for state contributions	37.80
	$ 4.20

The result was an increase in a liability of the employer.

(f) The amount credited to State Unemployment Contributions Payable was computed as follows:

2.7% of $1,400 = $37.80

The result was an increase in a liability of the employer.

(g) The amount credited to the bank was computed as follows:

Wages earned by employees	$1,400.00
Employees' tax withheld, 1½%	21.00
Net amount of wages paid to employees	$1,379.00

The result was a decrease in an asset of the employer.

In those states where employers are required to withhold a certain percentage of their employees' wages for unemployment compensation purposes, the additional amount withheld should be credited to State Unemployment Contributions Payable. The amount to be credited to the bank will then be correspondingly less. If, in the foregoing case, the employer had been required to withhold 1 per cent of his employees' wages for unemployment compensation purposes, it would be necessary to credit State Unemployment Contributions Payable for $14 more, or a total of $51.80 instead of $37.80. At the same time the bank would be credited for $14 less, or $1,365 instead of $1,379.

Disability Benefits. In addition to the social security taxes already discussed, some states impose taxes on employers and employees for sickness and disability benefits. Separate accounts should be kept to record such taxes, but the principles involved are the same as those already discussed. In other words, such taxes imposed on the employer should be recorded in both an expense account and a liability account. Any taxes that the employer is required to withhold from the employees' wages for disability benefits should be recorded by crediting a liability account.

PRACTICE ASSIGNMENT No. 33. Complete Report No. 33 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 34 is required.

XXXIV INCOME TAXES

Since March 1, 1913, the Federal Government has imposed a tax on income. A number of the states also impose a tax on income.

There have been frequent changes in the income tax laws with respect to the following factors:

(a) Taxable income.

(b) Allowable deductions.

(c) Credits.

(d) Rates of tax.

Under the present income tax law, taxpayers who are employers are not only required to pay a federal tax on their incomes; they are also required to assist the government in collecting the income taxes imposed on their employees. This is accomplished by withholding a portion of the wages paid to their employees.

Taxpayers are required to maintain accounting records and to make an annual return of their true income. Uniform methods of accounting are not prescribed for all taxpayers; however, each taxpayer is expected to adopt a system of accounting that in his judgment is best suited to his needs. Under the federal income tax law, individuals, partnerships, and corporations are required to file income tax returns.

Bases Upon Which Returns May Be Filed. The federal income tax law provides that income tax returns may be filed on the basis of either the calendar year or a fiscal year and on either the cash basis or the accrual basis. The net income must be computed upon the basis of a fixed period that usually is a period of twelve months, known as a taxable year. Once a taxpayer has adopted a method of accounting and a basis of filing income tax returns, a change may not be made therefrom without first obtaining the approval of the Commissioner of Internal Revenue. That is, if a taxpayer has adopted the calendar year basis of keeping accounts and of reporting income, a change cannot be made to a fiscal year basis without the approval of the Commissioner. Likewise, if a taxpayer has adopted the accrual basis of accounting and of reporting income, a change cannot be made therefrom without the approval of the Commissioner.

Time and Place for Filing Returns. Federal income tax returns must be filed on or before the fifteenth day of the third month following the close of the taxable year. Taxpayers who file their returns on the calendar year basis must file their returns on or before March 15 of the year following the close of the taxable year. Taxpayers who file their returns on a fiscal year basis must file their returns on or before the fifteenth day of the third month following the close of their taxable year. Delinquency in filing an income tax return may subject the taxpayer to severe penalties.

The federal income tax returns must be filed in the office of the collector of internal revenue for the district in which the taxpayer's principal place of business is located.

Accounting for Income Taxes. The status of a taxpayer as an employer or as an employee is a basic factor in the method to be used in accounting for income taxes. An employer may be a sole proprietor, a partnership, or a corporation. If the taxpayer is a sole proprietor or a partner, any compensation he may draw for services rendered the enterprise will not be subject to withholding for income tax purposes. If the taxpayer is an employee, his compensation will be subject to withholding for income tax purposes and all or part of his income taxes will be withheld at the source.

Individuals. Individuals who are required to file federal income tax returns are divided into two principal groups as follows:

(a) Those individuals who qualify and elect to have the collector of internal revenue determine their tax for them.

(b) Those individuals who determine their own tax.

Individuals belonging to the first group are permitted to use a simplified form for their returns setting forth (a) the total amount of their wages, (b) the total amount of taxes withheld from their wages by their employer, and (c) the total amount of their other income, if any.

Individuals belonging to the second group may be divided into two classes as follows:

(a) Those individuals who may ascertain their tax by reference to a table.

(b) Those individuals who are not permitted to ascertain their tax by reference to a table, but whose taxes must be computed by applying the prescribed rates of normal tax and surtax.

The obligation of an individual to file an income tax return depends upon the amount of his gross income. It may be necessary for him to file a return even though no tax is to be paid. In the cases of married couples, the spouses may elect to file separate returns or they may unite in filing a single return jointly regardless of whether both have taxable income or allowable deductions.

Prior to January 1, 1943, income taxes were payable in the year following the year in which the income was received or earned. In other words, out of the current year's income the taxpayer was required to pay the income taxes incurred in the preceding year. This plan proved satisfactory when the imposition of taxes was limited to persons of relatively large incomes. With the beginning of World War II the need on the part of the government for greatly increased revenue resulted in the enactment of tax laws imposing taxes on millions of persons with small incomes derived primarily from wages. With this development came a demand from taxpayers that some provision be made for paying the tax out of current income in the same year in which the liability is incurred. As the result of this demand, a law was enacted providing for the current payment of income taxes as follows:

(a) By requiring employers to withhold a percentage of the wages paid to their employees; and

(b) By requiring individuals to make quarterly payments currently of that portion of their estimated taxes that is not withheld from their wages.

An individual who is engaged in business and who has one or more persons in his employ is required to withhold for income tax purposes a percentage of his employees' wages in excess of their withholding exemptions. The amount withheld by the employer during each calendar quarter must be paid to the collector of internal revenue at the time of filing the quarterly return on or before the last day of the month following the close of the quarter. However, where the sum of the taxes imposed on the employer and his employees under the Federal Insurance Contributions Act plus the amount of the employees' income taxes withheld during the first or second months of any calendar quarter is more than $100, it must be paid to a Federal Reserve Bank or a U. S. depositary within fifteen days after the close of the month. The amount withheld during the third month of any calendar quarter may either be paid to a Federal Reserve Bank or a U. S. depositary by the fifteenth of the following month or it may be paid to the Collector of Internal Revenue at the time of filing the quarterly return on or before the last day of the month following the close of the calendar quarter.

An account with Employees' Income Taxes Payable should be kept, and this account should be credited for the total amount withheld each payday. The account should be debited for the amount paid to the depositary each month or to the collector each quarter. The account normally has a credit balance that represents the employer's liability for taxes withheld. The account will be in balance when the entire amount withheld has been paid. Assume that L. R. Smithson is engaged in business as a sole proprietor. The wages of his employees are paid on the fifteenth and last days of each month. For the pay period ended January 15 his payroll amounted to $800, from which he withheld a total of $78.50 for income tax purposes. This transaction was recorded as indicated by the following general journal entry:

Wages	$800.00	
Employees' Income Taxes Payable		$ 78.50
Bank		721.50
Semimonthly payroll.		

Assuming that the amount withheld from the wages paid on January 31 was the same, the account with Employees' Income Taxes Payable would have a credit balance on January 31 of $157. Since the taxes withheld during the month amounted to more than $100, payment to a Federal Reserve Bank or a U. S. depositary had to be made by the fifteenth of February. At the time of payment, the check issued was recorded as indicated by the following general journal entry:

Employees' Income Taxes Payable	$157.00	
Bank		$157.00
Paid income taxes withheld from wages.		

After this entry was posted, the account with Employees' Income Taxes Payable was in balance.

An employer is also liable for his own personal income taxes in addition to his liability for the income taxes that he is required to withhold from the wages paid to his employees. As an employer, no amount will be withheld at the source to pay any portion of his personal income taxes. Where an individual who is the sole proprietor of a business allows himself a salary or draws a specified sum periodically as remuneration for services rendered, the amount of such salary or remuneration is not subject to withholding for income tax purposes. Furthermore, such remuneration may not be deducted by the proprietor in computing his net income from the business for income tax purposes.

An employer who is a sole proprietor may have income from sources other than his business and he may have allowable deductions not related to his business. It is customary, therefore, to treat the income tax liability of a sole proprietor as a personal obligation and not as a business expense.

Every individual is required to file a declaration of his estimated tax for each taxable year if —

(a) his gross income from wages is expected to exceed $4,500 plus $600 for each exemption, or

(b) his gross income from all other sources is expected to exceed $100 and his total income is expected to amount to $600 or more.

Declarations of estimated tax must be filed on or before the fifteenth day of the third month of the taxable year, with certain exceptions. The purpose of such declarations is to determine the amount of the quarterly payments that must be made during the year. The amount to be paid in quarterly installments is the unpaid balance of the estimated tax. Since compensation only is subject to withholding, no part of the business income of a sole proprietor will be withheld for income tax purposes, but he is required to make quarterly payments of the estimated tax on such income. If he makes quarterly payments from business funds to apply on his estimated income tax, the amounts paid should be charged to his drawing account. Any additional amount paid at the time of filing his final return for the taxable year should likewise be charged to his drawing account.

Assume that, in addition to remitting the income taxes withheld from the wages of his employees, L. R. Smithson made quarterly payments amounting to $150 each to apply on his estimated personal income tax. Each quarterly payment was recorded as indicated by the following general journal entry:

L. R. Smithson, Drawing........................	$150.00	
Bank..		$150.00
Quarterly payment of estimated tax.		

Partnerships. Every partnership is required to file a federal income tax return annually regardless of the amount of its income. The return is in the nature of an information return, showing each partner's distributive share of the partnership net income. The net income of a partnership must be computed according to the income tax law regardless of the provisions of the partnership agreement. The individual partners must include their distributive shares of the partnership profits in their respective individual returns regardless of whether or not the profits are distributed by the partnership. While a partnership is required to file an income tax return annually, actually the tax is imposed on the individual partners and not on the partnership.

Partnerships that have one or more persons in their employ are required to withhold for income tax purposes a percentage of the wages paid to their employees. The liability of a partnership to withhold income taxes from the wages paid to employees and to make payment of the amounts withheld to the collector of internal revenue or to a U. S. depositary is the same as that of a sole proprietor. Amounts withheld each payday should be credited to an account with Employees' Income Taxes Payable, while amounts remitted to the collector or to a U. S. depositary, should be recorded as a debit to Employees' Income Taxes Payable.

A partner is not considered an employee of the partnership; hence, if he draws a specified sum periodically as remuneration for services rendered, the partnership is not required to withhold a percentage of such remuneration for income tax purposes. In the preparation of an income tax return a partnership is not permitted to claim as a deduction any remuneration paid or allowed to the partners.

Neither is a partnership permitted to claim a deduction for charitable contributions; however, each partner may claim as a deduction in his individual return his proportionate share of any charitable contributions made by the partnership. Thus, if a partnership makes total charitable contributions of $800 during the taxable year, a partner owning a one half interest in the partnership may add $400 of the partnership's contributions to his personal contributions and claim the total as a deduction in his individual return, subject only to the limitation of 15 per cent of his adjusted gross income.

To illustrate, it is assumed that J. A. Bryant owns a one half interest in the partnership of Bryant & Wood. His adjusted gross income for the taxable year amounted to a total of $11,500 including his distributive share of the partnership's net income. During the taxable year the partnership made charitable contributions totaling $1,000, while Bryant made personal contributions totaling $1,200. Fifteen per cent of $11,500 equals $1,725. This represents the maximum amount of charitable contributions that may be claimed as a deduction in Bryant's individual return. His personal contributions, $1,200, plus one half of the partnership's contributions, $500, equals $1,700. Since this amount does not exceed the limitation, Mr. Bryant may claim the entire amount as a deduction in his individual return.

Since partners are not considered employees of a partnership and no deduction for any compensation paid or allowed them may be claimed in computing the partnership's net income, the net income shown in the profit and loss statement may vary considerably from the net income shown in the partnership's income tax return.

To illustrate, it will be assumed that J. A. Bryant and W. L. Wood are equal partners in the partnership of Bryant & Wood. Each receives a salary of $5,000 a year. For the taxable year, the profit and loss statement showed a net income of $24,000 after treating partners' salaries amounting to $10,000 and charitable contributions amounting to $1,000 as operating expenses. Since neither partners' salaries nor charitable contributions may be claimed as a deduction in the income tax return, the net income shown in the partnership return will amount to $35,000, of which each partner's distributive share is $17,500. Thus, in preparing their individual returns, each partner must include in his return income amounting to $17,500 regardless of the salary received or the profits distributed by the partnership during the year. Of course, each partner may claim one half of the partnership's charitable contributions, or $500, as a deduction in his individual return.

A partnership may keep its accounts and report its income on one basis while the partners may prepare their personal income tax returns on a different basis. Thus, a partnership may keep its accounts on a fiscal year basis and file its income tax returns on the same basis, while the partners may file their personal tax returns on the calendar year basis.

Corporations. Every corporation not expressly exempt from the income tax must file a federal return annually regardless of the amount of its income. Corporations fully organized must file a return whether they are doing business or not. However, a corporation that has received a charter but has never perfected its organization, has transacted no business, and has received no income from any source may be relieved from the necessity of making a return so long as it remains in an unorganized condition. Corporations in existence a part of a year only must file a return for that portion of the year.

Corporation returns must be filed on or before the fifteenth day of the third month following the close of the taxable year. The tax may be paid in full at the time of filing the return or it may be paid in installments, the first installment being paid at the time of filing the return. Under the Revenue Act of 1950 provision was made for corporations to pay their income taxes in installments as follows:

Calendar Year Ending	1st Installment		2nd Installment		3rd Installment		4th Installment	
	%	Payable	%	Payable	%	Payable	%	Payable
12-31-50	30	3-15-51	30	6-15-51	20	9-15-51	20	12-15-51
12-31-51	35	3-15-52	35	6-15-52	15	9-15-52	15	12-15-52
12-31-52	40	3-15-53	40	6-15-53	10	9-15-53	10	12-15-53
12-31-53	45	3-15-54	45	6-15-54	5	9-15-54	5	12-15-54
12-31-54	50	3-15-55	50	6-15-55				

In the case of corporations filing returns on a basis of fiscal years rather than calendar years, the first installment of the tax must be paid on the fifteenth day of the third month, the second installment on the fifteenth day of the sixth month, the third installment on the fifteenth day of the ninth month, and the fourth installment on the fifteenth day of the twelfth month following the close of the taxable year.

Since a corporation does not file its return until after the close of the year, it is customary to estimate the amount of the tax accrued at the end of the year and to record the estimated tax by debiting Federal Income Taxes and by crediting Federal Income Taxes Payable. Payments made to apply on the tax should then be recorded by debiting Federal Income Taxes Payable and by crediting the bank account.

The officers of a corporation are considered employees and their salaries are subject to withholding for income tax purposes the same as salaries or wages paid to other employees. Accounting for the taxes withheld by a corporation from the wages of its employees is the same as for a sole proprietor or a partnership. It is considered desirable to segregate the corporation's liability for the taxes withheld from the wages of its employees from the corporation's liability for its own income taxes; hence, separate accounts should be kept under appropriate titles. For example, the taxes withheld from the wages of its employees may be credited to an account with Employees' Income Taxes Payable, while the estimated amount of the corporation's own income taxes may be credited to an account with Federal Income Taxes Payable.

Taxes imposed on corporations under the federal social security law, unemployment contributions required of corporations under state unemployment compensation laws, property taxes imposed on corporations by state and local governments, state income taxes imposed on corporations, and state sales taxes paid by corporations are expenses that may be claimed as deductions in the corporation's federal income tax returns. Such taxes should, therefore, be considered operating expenses.

Assume that, before closing its books at the end of a year, a corporation estimates that its federal income tax will amount to $14,000. The tax should be recorded as indicated in the following general journal entry:

Federal Income Taxes......................	$14,000.00	
Federal Income Taxes Payable............		$14,000.00
Estimated federal income taxes.		

The amount charged to Federal Income Taxes should be listed in the corporation's profit and loss statement as a deduction from net income, while the amount credited to Federal Income Taxes Payable should be listed in the balance sheet as a current liability.

If a corporation is also subject to state income taxes, such taxes may be recorded similarly. However, the expense and the liability accounts for state income taxes should be kept separate from accounts used to record federal income taxes, as it is not advisable to record both federal and state income taxes in the same accounts.

PRACTICE ASSIGNMENT No. 34. Complete Report No. 34 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 35 is required.

XXXV SALES TAXES AND PROPERTY TAXES

Sales Taxes. Most of the states and some cities impose either sales taxes or gross receipts taxes. The tax is imposed either on the consumer or on the vendor. The following is a brief summary of the different types of sales taxes:

(a) A consumer sales tax under which the distributor is required to collect the tax. The tax is based on the selling price of the merchandise.

(b) A gross receipts sales tax under which the distributor collects the tax from the consumer. The tax is based on a certain percentage of receipts from taxable sales and is remitted periodically to the state by the distributor.

(c) A gross receipts sales tax under which the distributor pays the tax but is not permitted to collect it directly from the consumer.

In states in which there is a gross receipts sales tax, the amount of the tax is computed as a certain percentage of the gross receipts from taxable sales. In several states, including Kansas, Illinois, Iowa, Michigan, North Dakota, South Dakota, and Oklahoma, the sales tax is based on the gross receipts from taxable sales. Usually the tax is payable quarterly, sometime during the month following the close of each calendar quarter.

Accounting for Sales Taxes. The method of accounting for sales taxes depends upon the manner in which the tax is imposed. If the tax is imposed on the consumer and the vendor is required to collect it and remit it to the state or the city, it is necessary for the vendor to keep a record of the tax so that he will have the information needed in preparing the periodic reports and in remitting the amount due the state or the city.

On cash sales the tax is collected at the time of the sale. A record is kept of the total amount collected and this amount is entered daily or periodically in the record of cash receipts. On charge sales the tax is added to the invoice as an additional charge to the customer. It is usually listed separately as shown in Illustration No. 54.

To facilitate the recording of sales taxes on charge sales, a special column may be added to the sales record as illustrated on page 467. It will be noted that the sales invoice reproduced in Illustration No. 54 has been recorded in the sales record. All charge sales invoices should be recorded in a similar manner. At the end of the month when the summary posting is completed, the total of the Sales Tax column should be posted to the credit of Sales Tax Payable. At the same time the total sales tax on cash sales will be posted to the sales tax payable account from the cash

SALES RECORD FOR MONTH OF *MAY* 19--

DEBITS: General Ledger Acct. No.	DEBITS: General Ledger Amount	DEBITS: General Ledger ✓	DEBITS: Accounts Receivable	✓	Day	Name	Sale No.	CREDITS: Sales Dept. A	CREDITS: Sales Dept. B	CREDITS: Sales Tax	CREDITS: Trans. Out	CREDITS: General Ledger Acct. No.	CREDITS: General Ledger Amount	CREDITS: General Ledger ✓
						Amounts Forwarded								
			93 83	✓	*14*	*Walter Burns*	*629*		*91 10*	*2 73*				

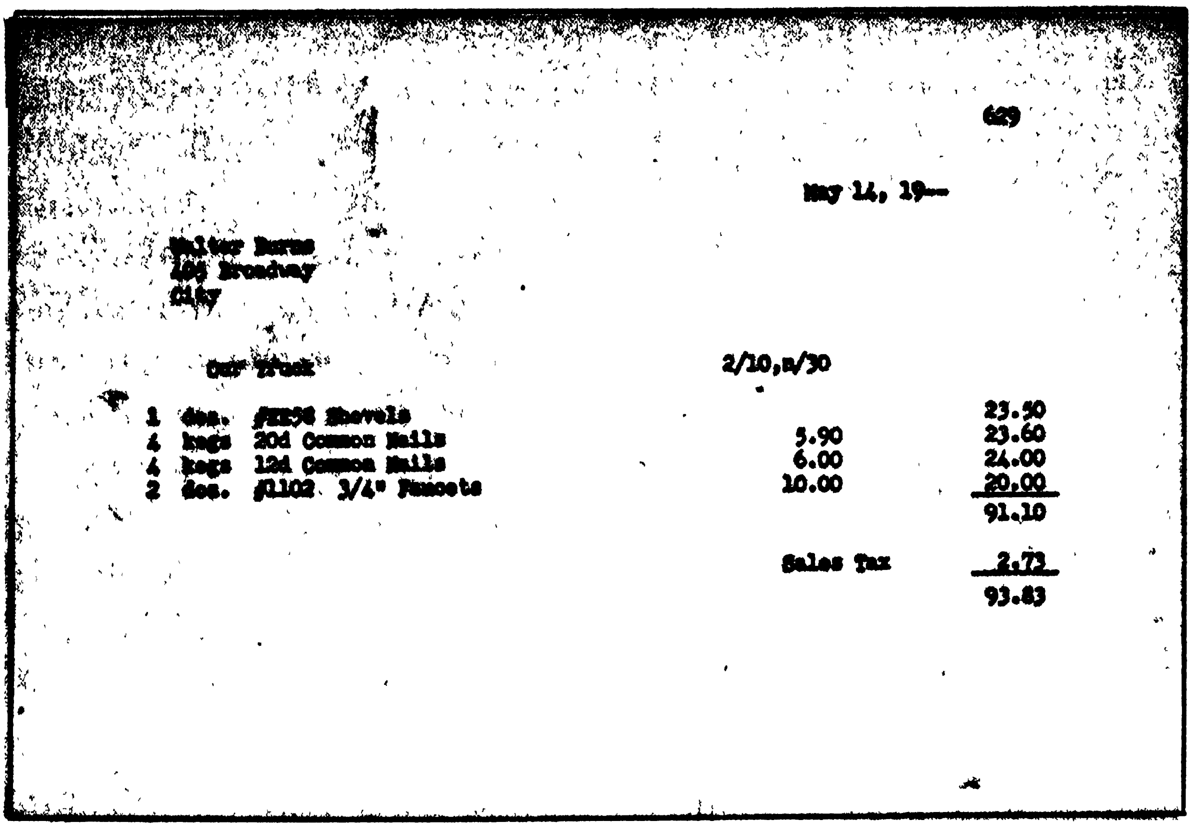
receipts record. After all posting has been completed, the credit balance of the sales tax payable account will represent the total amount due the state on account of sales taxes imposed on both cash and charge sales. When the tax is remitted to the state, the payment should be entered in the record of cash payments by debiting Sales Tax Payable and by crediting the bank account. The sales tax payable account should be in balance when all of the tax collected from customers has been remitted to the state.

In posting from the sales invoices to the individual accounts of customers in the accounts receivable ledger, the amount of the sale and the amount of the sales tax are usually posted as separate items. If cash discounts are offered for payment within a specified time, the amount of the sale would be subject to the discount, but any amount added to the invoice on account of sales tax imposed on the customer would not be subject to discount.

A series of transactions will serve to illustrate the method suggested for recording sales taxes imposed on the consumer and collected by the vendor.

January 31. A merchant sold Lawrence Peck a piano for $700 on which the sales tax at 3 per cent amounted to $21.

This transaction was entered in the sales record by debiting Lawrence Peck for $721 and by crediting Sales Taxes Payable for $21 and Sales for $700.



629

May 14, 19—

Walter Burns
[illegible] Broadway
City

Our Truck

2/10,n/30

1	doz.	[illegible] Shovels		23.50
4	kegs	20d Common Nails	5.90	23.60
4	kegs	12d Common Nails	6.00	24.00
2	doz.	#1102 3/4" Faucets	10.00	20.00
				91.10
			Sales Tax	2.73
				93.83

Illustration No. 54, Carbon Copy of Sales Invoice Including Sales Tax

February 15. The merchant received a check from Lawrence Peck for $721 in full payment of his account.

This transaction was entered in the record of cash receipts by debiting the bank account and by crediting Lawrence Peck for $721.

April 30. The merchant filed his state sales tax report for the quarter ended March 31 and paid the taxes due.

Assuming that the sale on January 31 was the only taxable sale during the quarter ended March 31, the payment of the sales tax may be entered in the record of checks drawn by debiting Sales Taxes Payable and by crediting the bank account. After all of these transactions have been recorded, the account with Lawrence Peck will be in balance and the account with Sales Taxes Payable will be in balance also.

In states where the vendor is required to purchase sales tax stamps, the amount paid for stamps should be recorded by debiting Sales Tax Stamps and by crediting the bank account. When taxable sales are made for cash, the tax is collected from the customer and he is given canceled stamps for the amount of the tax. When taxable sales are made on account, the customer is charged for both the sales price of the merchandise and the amount of the tax and is given canceled tax stamps. In recording cash sales, the bank account should be debited for the amount received, Sales should be credited for the selling price of the merchandise, and Sales Tax Payable should be credited for the amount of the tax. In recording charge sales, the customer should be debited for the total amount to be charged to his account, Sales should be credited for the selling price of the merchandise, and Sales Tax Payable should be credited for the amount of the tax.

At the end of each month or each accounting period, an inventory of the unused sales tax stamps should be taken and an adjusting entry should be made debiting Sales Tax Payable and crediting Sales Tax Stamps for the amount of the stamps used. After this entry is posted, the debit balance of the sales tax stamps account will be the value of the unused stamps on hand. This represents an asset that is usually listed as a prepayment among the current assets in the balance sheet.

Property Taxes. In most states taxes are imposed on both real and personal property. Usually the revenue from such taxes goes to the local subdivisions including the counties, townships, municipalities, school districts, etc. There is a wide variation in the administration of property taxes in the different states. Usually the taxes are assessed as of a certain date and become a lien on the property until the tax is paid in full. In most states property taxes may be paid in two or more installments if desired. In Ohio, for example, the full amount of the real property tax may be paid on or before December 20, or one half thereof may be paid before December 20 and the remaining half before June 20 next ensuing, or the taxpayer may elect to pay the full amount in ten equal installments, the first of which is payable on or before December 20 and the remaining installments on or before the tenth day of each succeeding month.

Accounting for Property Taxes. Accounting for property taxes is relatively simple. Each accounting period should be charged with its proper portion of all property taxes. Under the accrual method of keeping accounts, any taxes that have been assessed but not paid at the end of the accounting period should be set up as accrued property taxes payable. Assuming that real property taxes are payable in two installments, the first installment being due on December 20 and the second installment on June 20 of the ensuing year, and that the total taxes assessed in a given year amounted to $180, the transactions involved may be recorded in general journal form as follows:

Dec. 20.	Property Taxes	$90.00	
	Bank		$90.00
	Paid the first half of the property taxes assessed for the year ending December 31.		

Dec. 31.	Property Taxes	$90.00	
	Accrued Property Taxes Payable		$90.00
	Property taxes accrued on December 31.		

When these entries are posted to the proper accounts, the account with Property Taxes will have a debit balance of $180, which represents the correct amount of the expense incurred on account of property taxes assessed for the year ending December 31. The accrued property taxes payable account will have a credit balance of $90, which represents the amount of the unpaid taxes that should appear in the balance sheet as a current liability. When the second half of the taxes is paid, the entry may be recorded in general journal form as follows:

June 20.	Accrued Property Taxes Payable	$90.00	
	Bank		$90.00
	Paid the second half of the property taxes assessed for previous year.		

When this entry is posted, the accrued property taxes payable account will be in balance.

In some cases the entire amount of the real and personal property taxes will be set up at the time the taxes are assessed by debiting Property Taxes and by crediting Accrued Property Taxes Payable. Then, as each payment is made, it will be recorded by debiting Accrued Property Taxes Payable and by crediting the bank account.

No general method of accounting for property taxes can be prescribed without taking into consideration the laws of the state in which the taxpayer is located. However, the amount of tax assessed for any year represents an operating expense of that year and the unpaid portion of the assessed tax at the end of the year represents a current liability.

PRACTICE ASSIGNMENT No. 35. Complete Report No. 35 in the workbook and submit your working papers to the instructor for approval. Then continue with the next study assignment in Unit Seventeen until Report No. 36 is required.

Unit Seventeen

A SYSTEM OF ACCOUNTS FOR A WHOLESALE MERCHANT

XXXVI APPLICATION OF ACCOUNTING PRINCIPLES

In a wholesale merchandising enterprise, the merchandise handled is usually purchased direct from the manufacturers, importers, or producers and is sold to retailers and distributors, who in turn sell to consumers at retail prices. The wholesaler usually buys in large quantities and has storage facilities to enable him to carry a large stock of merchandise from which he may supply his customers in the desired quantities. The wholesaler may purchase the goods he handles for cash or on credit and, likewise, he may sell the goods for cash or on credit. A large percentage of the wholesale business is on a credit basis.

The books of account and the auxiliary records of a wholesale merchant will vary depending upon a number of factors such as the following:

(a) Type of business organization.
(b) Nature of the business.
(c) Volume of business.
(d) Office equipment.
(e) Information desired on the part of the management and others concerned with the operation of the business.

Type of Business Organization. A wholesale merchandising enterprise may be conducted as a sole proprietorship, a partnership, or a corporation. So far as the sole proprietorship and the partnership forms of organization are concerned, there are no distinctive records to be kept. Under the corporate form of organization, certain corporate records such as a minute book, a stock certificate record, and a stockholders' ledger may be kept. The type of organization will usually affect the chart of accounts also. In the case of a sole proprietorship, it may be necessary to keep two proprietorship accounts only — one for recording the proprietor's capital and the other for recording the proprietor's personal transactions. In the case of a partnership, it is necessary to keep separate proprietorship accounts for each partner in order that each partner's capital or net worth may be ascertained at any time. In the case of a corporation, it is necessary to keep separate accounts for capital stock, surplus, and dividends payable.

Nature of the Business. The system of accounts may vary considerably, depending upon the nature of the business enterprise; for example, the transactions of a mercantile enterprise may be quite different from the transactions of a service enterprise. The sources of income and the types of expenses incurred may vary with the nature of the business. Some businesses are of such a nature that it is advisable to keep the accounts on a departmental basis in order that the results of operating each department may be ascertained. In some businesses it is customary to buy and sell for cash only; in some it is customary to buy and sell for both cash and on credit; and in others it may be customary to sell on the installment basis. The accounts of a mercantile enterprise selling on the installment basis may be kept on either the usual accrual basis or the installment basis at the option of the proprietor.

Volume of Business. The size of a firm and the volume of its business are important factors in determining the extent to which the records and the accounts should be subdivided. Obviously, the records and the accounts of a firm doing a million dollar business annually will vary considerably from those of a firm doing a $50,000 business. In a big business with numerous departments, there will be a demand for more statistical information and a greater need for adequate control.

The number of employees usually is affected by the size or the volume of the business. With an increase in the number of employees in the accounting department will come the need for a subdivision of both the books of original entry and the books of final entry. What is sometimes called the *unit system of accounting* is usually employed in such cases, the records being subdivided on a functional basis. Under this system a separate record is kept of each type of transaction. For example, all incoming purchase invoices are entered in an invoice record; sales invoices are entered in a sales record; cash receipts are entered in a record of cash receipts; and checks issued are entered in a record of checks drawn. Miscellaneous transactions that cannot be entered in the special journals are entered in a general journal.

The unit system of accounting offers the following advantages:

(a) Provides for a better internal check and control.

(b) Makes possible an equitable distribution of work among several employees.

(c) Provides for a more detailed classification of transactions in the books of original entry.

(d) Facilitates summary posting periodically to the general ledger accounts.

Office Equipment. The accounting system is certain to be affected by the use of various types of office machines. In recent years there has been a great expansion in the various types of accounting, calculating, and other office machines. In the modern office of a big business enterprise, it is not uncommon in these times to find a large percentage of the accounting work being done with the aid of mechanical devices, including posting machines, electric accounting machines, and photographic equipment.

Regardless of the number of machines employed in the accounting department, the fundamental principles involved in keeping the accounts are not affected. A knowledge of accounting theory is just as essential on the part of those employed in the accounting department as if no machines were used.

Information Desired. The accounting system must be designed to provide the management and others concerned with the operation of a business with the desired information. The management not only may wish to know where the business stands financially from time to time, but also will surely want to know the results of operations over given periods of time. The accounting department may be required to supply much information of a statistical nature as well as the usual accounting reports. For example, the manager of the purchasing department may expect the accounting department to keep detailed stock records of all merchandise handled. The accounts must be kept so as to provide all the information needed for all the various tax reports required by the federal, state, and local governments. In recent years there has been a tremendous increase in the number of tax reports and the amount of tax information that must be furnished. Many large firms have found it necessary to organize a tax accounting department separate from the general accounting department. The work of the tax accounting department may be confined to the handling of federal and state social security tax reports, or the scope of its work may be extended to all tax reports including income taxes, sales taxes, excise taxes, property taxes, corporation franchise taxes, etc.

Application of Principles. Bryant & Wood are partners conducting a wholesale automobile accessory business. The merchandise handled consists of (a) tires and tubes and (b) radios and batteries. The merchandise is purchased from various manufacturers and producers and is sold to local dealers and distributors. Most of the merchandise is purchased on credit, but occasionally goods may be purchased for cash. The merchandise is sold both for cash and on credit. On credit purchases the terms may vary considerably. Most of the firms from whom Bryant & Wood buy allow discounts ranging from 1 to 3 per cent for cash in from 10 to 30 days. On credit sales the terms usually are 2 per cent discount for cash in 10 days, net 30 days.

The unit system of accounting is used by Bryant & Wood and their books of account consist of the following:

(a) Books of original entry
- (1) Invoice record
- (2) Sales record
- (3) Record of cash receipts
- (4) Record of checks drawn
- (5) General journal

(b) Books of final entry
- (1) General ledger
- (2) Accounts receivable ledger
- (3) Accounts payable ledger
- (4) Operating expense ledger

(c) Auxiliary records
- (1) Petty cash disbursements record
- (2) Stock record
- (3) Fixed asset record
- (4) Notes receivable register
- (5) Insurance policy register
- (6) Daily bank statement
- (7) Bank passbook

Invoice Record. A comparison of Bryant & Wood's invoice record reproduced on page 496 with the invoice record reproduced on page 341 will reveal that they are identical. This form of invoice record was described in detail in Unit Twelve.

Sales Record. A comparison of Bryant & Wood's sales record reproduced on page 497 with the sales record reproduced on page 365 will reveal that they are identical. This form of sales record was described in detail in Unit Thirteen.

Record of Cash Receipts. Bryant & Wood keep a columnar record of cash receipts. Reference to the record of cash receipts reproduced on page 498 will reveal that General Ledger Dr. and Cr. columns are provided. In addition, special amount columns are provided for (a) Sales Discount Dr., (b) Bank Dr., (c) Accounts Receivable Cr., and (d) Cash Sales, Depts. A and B, Cr. All cash and cash items received are recorded by debiting the bank account immediately. This practice is usually followed where it is the custom to deposit all cash receipts in a bank and to make all disbursements by check.

Proving the Record of Cash Receipts. The record of cash receipts may be footed and the footings may be proved daily or periodically by comparing the sum of the debit footings with the sum of the credit footings. When a page has been filled, the amount columns should be footed, the footings should be proved, and the totals should be carried forward to the top of the next page. It is customary to start a month at the top of a new page.

Posting from the Record of Cash Receipts. Completing the posting from the record of cash receipts involves both individual posting and summary posting. Individual posting is required from the General Ledger Dr. and Cr. columns. This posting is usually done daily. As each item is posted, a check mark should be entered in the Check ($\surd$) column following the Amount column of the record of cash receipts; the initials "CR" and the page number of the record of cash receipts should be entered in the Folio column of the proper general ledger account preceding the amount posted.

The summary posting is usually completed at the end of each month and involves the following procedure:

(a) The total of the column headed Sales Discount should be posted to the debit of Sales Discount, Account No. 751, in the general ledger.

(b) The total of the column headed Bank should be posted to the debit of Liberty National Bank, Account No. 111, in the general ledger.

(c) The total of the column headed Accounts Receivable should be posted to the credit of Accounts Receivable, Account No. 132, in the general ledger.

(d) The total of the column headed Cash Sales, Dept. A, should be posted to the credit of Sales, Dept. A, Account No. 511, in the general ledger.

(e) The total of the column headed Cash Sales, Dept. B, should be posted to the credit of Sales, Dept. B, Account No. 512, in the general ledger.

As the total of each column is posted, the account number should be written immediately below the total in the record of cash receipts; the page number of the record of cash receipts should be entered in the Folio column of the proper general ledger account as a cross reference. A check mark should be placed below the totals of the General Ledger Dr. and Cr. columns to indicate that these totals need not be posted.

Record of Checks Drawn. Bryant & Wood keep a columnar record of checks drawn. Reference to the record of checks drawn reproduced on pages 499 and 500 will reveal that General Ledger Dr. and Cr. columns are provided. In addition, special amount columns are provided for (a) Operating Expenses Dr., (b) Accounts Payable Dr., (c) Purchases Discount Cr., and (d) Bank Cr.

Proving the Record of Checks Drawn. The record of checks drawn may be footed and the footings may be proved daily or periodically by comparing the sum of the debit footings with the sum of the credit footings. When a page has been filled, the amount columns should be footed, the footings should be proved, and the totals should be carried forward to the top of the next page. It is customary to start a month at the top of a new page.

Posting from the Record of Checks Drawn. Completing the posting from the record of checks drawn involves both individual posting and summary posting. Individual posting is required from the General Ledger Dr. and Cr. columns. This posting is usually done daily. As each item is posted, a check mark should be entered in the Check (√) column following the Amount column of the record of checks drawn; the initials "CD" and the page number of the record of checks drawn should be entered in the Folio column of the ledger account preceding the amount posted.

Individual posting is also required from the Operating Expenses Dr. column. This posting is usually done daily. As each item is posted, a check mark should be entered in the Check (√) column following the Amount column of the record of checks drawn; the initials "CD" and the page number of the record of checks drawn should be entered in the Folio column of the proper operating expense ledger account preceding the amount posted.

The summary posting is usually completed at the end of each month and involves the following procedure:

(a) The total of the Operating Expenses Amount column should be posted to the debit of Operating Expenses, Account No. 71, in the general ledger.

(b) The total of the column headed Accounts Payable should be posted to the debit of Accounts Payable, Account No. 36, in the general ledger.

(c) The total of the column headed Purchases Discount should be posted to the credit of Purchases Discount, Account No. 521, in the general ledger.

(d) The total of the column headed Bank should be posted to the credit of Liberty National Bank, Account No. 111, in the general ledger.

As the total of each column is posted, the account number should be written immediately below the total in the record of checks drawn; the page number of the record of checks drawn should be entered in the Folio column of the proper general ledger account as a cross reference. A check mark should be placed below the totals of the General Ledger Dr. and Cr. columns to indicate that these totals need not be posted.

General Journal. Bryant & Wood use a columnar general journal. Reference to the general journal reproduced on page 501 will reveal that General Ledger Dr. and Cr. columns are provided. In addition, special amount columns are provided for (a) Operating Expenses Dr., (b) Accounts Payable Dr., (c) Accounts Payable Cr., and (d) Accounts Receivable Cr. The general journal is used for recording all transactions that cannot be recorded in the special journals. It is also used for recording the adjusting entries required at the end of each month and for recording the closing entries required at the end of each year.

Proving the General Journal. The general journal may be footed and the footings may be proved daily or periodically by comparing the sum of the debit footings with the sum of the credit footings. When a page has been filled, the amount columns should be footed, the footing should be proved, and the totals should be carried forward to the top of the next page. It is customary to start a month at the top of a new page.

Posting from the General Journal. Completing the posting from the general journal involves both individual posting and summary posting. Individual posting is required from the General Ledger Dr. and Cr. columns. This posting is usually done daily. As each item is posted, a check mark should be entered in the Check (√) column following the Amount column of the general journal; the initials "GJ" and the page number of the general journal should be entered in the Folio column of the proper general ledger account preceding the amount posted.

Individual posting is also required from the Operating Expenses Dr. column. As each item is posted, a check mark should be entered in the Check (√) column following the Amount column of the general journal; the initials "GJ" and the page number of the general journal should be entered in the Folio column of the proper operating expense ledger account preceding the amount posted.

The summary posting is usually completed at the end of each month and involves the following procedure:

(a) The total of the Operating Expenses Amount column should be posted to the debit of Operating Expenses, Account No. 71, in the general ledger.

(b) The total of the debit column headed Accounts Payable should be posted to the debit of Accounts Payable, Account No. 36, in the general ledger.

(c) The total of the credit column headed Accounts Payable should be posted to the credit of Accounts Payable, Account No. 36, in the general ledger.

(d) The total of the column headed Accounts Receivable should be posted to the credit of Accounts Receivable, Account No. 132, in the general ledger.

As the total of each column is posted, the account number should be written immediately below the total in the general journal; the page number of the general journal should be entered in the Folio column of the proper general ledger account as a cross reference. A check mark should be placed below the totals of the General Ledger Dr. and Cr. columns to indicate that these totals need not be posted.

General Ledger. Bryant & Wood use a general ledger containing standard ledger ruled paper. The accounts are arranged in this ledger in numerical order. A chart of the accounts is reproduced on page 479. It will be noted that the accounts are numbered and classified.

All posting to the general ledger accounts is done from the books of original entry. As each item is posted, the page of the journal from which it is posted is entered in the Folio column of the account.

BRYANT & WOOD

CHART OF GENERAL LEDGER ACCOUNTS

Note: Items in italics represent headings and not account titles.

I Current Assets

- *11 Cash*
  - 111 Liberty National Bank
  - 112 Petty Cash Fund
- 12 U. S. Treasury Bonds
- *13 Receivables*
  - 131 Notes Receivable
  - 132 Accounts Receivable
    - 013 Reserve for Bad Debts
- 14 Mdse. Inventory, Dept. A
- 15 Mdse. Inventory, Dept. B
- 16 Accrued Interest Receivable
- *17 Supplies and Prepayments*
  - 171 Store Supplies
  - 172 Advertising Supplies
  - 173 Office Supplies
  - 174 Postage Stamps
  - 175 Prepaid Insurance
  - 176 Prepaid Federal Excise Tax

II Fixed Assets

- 21 Store Equipment
  - 021 Res. for Depr. of Store Equipment
- 22 Delivery Equipment
  - 022 Res. for Depr. of Del. Equipment
- 23 Office Equipment
  - 023 Res. for Depr. of Office Equipment

III Current Liabilities

- 31 Federal Old-Age Ins. Taxes Pay.
- 32 Federal Unemployment Taxes Payable
- 33 State Unemployment Contributions Payable
- 34 Employees' Income Taxes Pay.
- 35 Notes Payable
- 36 Accounts Payable
- 37 Accrued Interest Payable
- 38 Accrued Property Taxes Pay.

IV Proprietorship

- 41 J. A. Bryant, Partner
- 411 J. A. Bryant, Drawing
- 42 W. L. Wood, Partner
- 421 W. L. Wood, Drawing
- 43 Profit and Loss Summary

V Income

- *51 Operating Income*
  - 511 Sales, Dept. A
    - 0511 Sales R. & A., Dept. A
  - 512 Sales, Dept. B
    - 0512 Sales R. & A., Dept. B
- *52 Financial Income*
  - 521 Purchases Discount
  - 522 Interest Income

VI Costs

- 61 Purchases, Dept. A
  - 061 Pur. R. & A., Dept. A
- 62 Purchases, Dept. B
  - 062 Pur. R. & A., Dept. B
- 63 Transportation In, Dept. A
- 64 Transportation In, Dept. B
- 65 Cost of Sales, Dept. A
- 66 Cost of Sales, Dept. B

VII Expenses

- 71 Operating Expenses
- *75 Financial Expenses*
  - 751 Sales Discount
  - 752 Interest Expense
  - 753 Charitable Contributions
  - 754 Collection Expense

Accounts Receivable Ledger. Bryant & Wood use an accounts receivable ledger containing balance-column ledger ruled paper. The accounts are arranged in this ledger in alphabetic order. A control account for accounts receivable (Account No. 132) is kept in the general ledger. At the end of each month it is customary to prepare a schedule of the accounts receivable, the total of which should be the same as the balance of the accounts receivable control account.

Posting to the customers' accounts in the accounts receivable ledger may be done either from the books of original entry or direct from vouchers or other documents that represent the transactions. The accountant for Bryant & Wood follows the latter practice.

Accounts Payable Ledger. Bryant & Wood use an accounts payable ledger containing balance-column ledger ruled paper. The accounts are arranged in this ledger in alphabetic order. A control account for accounts payable (Account No. 36) is kept in the general ledger. At the end of each month it is customary to prepare a schedule of the accounts payable, the total of which should be the same as the balance of the accounts payable control account.

Posting to the creditors' accounts in the accounts payable ledger may be done either from the books of original entry or direct from vouchers or other documents that represent the transactions. The accountant for Bryant & Wood follows the latter practice.

Operating Expense Ledger. Bryant & Wood use an operating expense ledger containing balance-column ledger ruled paper. The accounts are arranged in this ledger in numerical order. A chart of the accounts is reproduced on page 481. A control account for operating expenses (Account No. 71) is kept in the general ledger. At the end of each month, after any needed adjustments in the operating expense accounts are made, it is customary to prepare a schedule of the operating expenses. The total of this schedule should be the same as the balance of the operating expense control account.

All posting to the operating expense accounts is done from the books of original entry. As each item is posted, the page of the journal from which it is posted is entered in the Folio column of the account.

Auxiliary Records. Bryant & Wood keep certain auxiliary records, including a petty cash disbursements record, a stock record, a fixed asset record, a notes receivable register, an insurance policy register, a daily

BRYANT & WOOD

CHART OF OPERATING EXPENSE LEDGER ACCOUNTS

Selling Expenses		*Administration Expenses*	
711	Advertising Expense	731	Rent
712	Salaries of Store Clerks	732	J. A. Bryant, Salary
713	Wages of Truck Driver	733	Office Salaries
714	W. L. Wood, Salary	734	Light and Water
715	W. L. Wood, Traveling Exp.	735	Telephone and Telegrams
716	Gas and Oil for Truck	736	Loss on Bad Debts
717	Repairs on Truck	737	Property Taxes
718	Garage Rent	738	Office Supplies Consumed
719	Transportation Out	739	Postage
720	Expired Insurance on Mdse.	740	Expired Ins. on Office Equip.
721	Expired Ins. on Del. Equip.	741	Depreciation of Office Equip.
722	Expired Ins. on Store Equip.	742	Social Security Taxes
723	Store Supplies Consumed	743	State Unemp. Contributions
724	Postage	744	Miscellaneous Gen. Expense
725	Depreciation of Store Equip.		
726	Depreciation of Del. Equip.		
727	Miscellaneous Selling Expense		

bank statement, and a bank passbook. The form of the petty cash disbursements record is similar to that shown on page 119. Their record of petty cash disbursements for May is reproduced on page 502. The form of the fixed asset record is similar to that shown on page 432. The form of the notes receivable register is similar to that shown on pages 398 and 399. The form of the insurance policy register is similar to that shown on pages 424 and 425.

Stock Record. Bryant & Wood keep a stock record as a means of control and as an aid to good business management. Many merchants follow a practice of having financial statements prepared monthly even though the accounts may be kept on the basis of an annual accounting period. Usually it is impractical to take a physical inventory monthly; hence a merchant may rely on his stock record for ascertaining the inventories needed for monthly statements. Even though a stock record or perpetual inventory is kept, it is advisable to take a physical inventory at the end of each year, at which time the stock records should be adjusted for any discrepancies that may be found to exist.

One form of stock record is shown in Illustration No. 55. The information needed in keeping such a record is obtained from the purchase invoices, sales invoices, charge-back invoices, and credit memorandums. In recording receipts, sales, returns, and balances, only quantities are entered. Minimum quantities are indicated and, whenever the quantity in stock reaches the minimum, the purchasing department is notified.

STOCK RECORD

Date	Inv. No.	Received	Issued	Balance	Date	Inv. No.	Received	Issued	Balance
19— Apr. 1				50					
5	S810		2	48					
11	S811		7	41					
15	S812		3	38					
18	P89	12		50					
20	Cr.23	2		52					
25	S813		25	27					
26	S814		7	20					
27	PB14		4	16					
28	P90	24		40					
30	Totals	38	48	40					

Article	Description	Minimum	Dept.
DeLuxe Tire	6.70-15 4-Ply	45	A

Illustration No. 55, Stock Record

Daily Bank Statement. Bryant & Wood keep a daily record of banking transactions known as a daily bank statement. Their May statement is reproduced on page 503. It will be noted that in addition to providing amount columns for recording the total deposits each day, the total checks written each day, and the bank balance at the end of each day, provision is made for a monthly bank reconciliation. This statement eliminates the need for keeping a record of the bank balance on the stubs of the checkbook.

Checkbook. Bryant & Wood use a checkbook bound with three checks to a page with stubs attached. The purpose of the stubs is to provide spaces for recording the information needed in recording the checks in the record of checks drawn and in posting to the accounts with creditors in the accounts payable ledger.

Accounting Procedure. The accounts of Bryant & Wood are being kept on the basis of a fiscal year ending June 30. The books of original entry, including the invoice record, the sales record, the record of cash receipts, the record of checks drawn, and the general journal, are reproduced in the illustrations on pages 496 to 501 inclusive. The only auxiliary records reproduced are the petty cash disbursements record, page 502, and the daily bank statement, page 503. The general and subsidiary ledgers are not reproduced. Following is a narrative of the May transactions that are shown recorded in the illustrations:

NARRATIVE OF TRANSACTIONS

BRYANT & WOOD, WHOLESALE DEALERS IN AUTOMOBILE ACCESSORIES

Monday, May 1

Issued Check No. 430 for $300 to H. H. Davids in payment of the May rent.

Received a check for $418.65 from W. O. Davenport in payment of our invoice of April 21 for $426.50, less 2% discount.

Before recording the check received from W. O. Davenport, it was reconciled by referring to his account in the accounts receivable ledger. The account showed that on April 21 he had been charged for merchandise amounting to $392.38 and for federal excise tax amounting to $34.12. A discount of 2% is allowed for cash in ten days, but of course the excise tax is not subject to any discount. The amount of his remittance was therefore verified in the following manner:

Merchandise sold	$392.38
Less 2% discount	7.85
	$384.53
Plus federal excise tax	34.12
Net amount due	$418.65

When the check was found to be for the proper amount, it was posted immediately to the credit of the account with W. O. Davenport in the accounts receivable ledger, the amount of the check, $418.65, being entered on one line and the amount of the discount, $7.85, being entered on the next line. The check was then entered in the record of cash receipts by debiting the bank account for the amount of the check, $418.65, by debiting Sales Discount for the amount of the discount, $7.85, and by crediting Accounts Receivable for the total of the invoice, $426.50. A check mark was placed in the Check (√) column following the amount entered in the Accounts Receivable column to indicate that the posting to W. O. Davenport's account had been completed.

Made charge sale as follows:

No. 815, W. O. Davenport, Jackson; tires and tubes, $148.76, federal excise tax, $12.94; radio and batteries, $84.20; express collect; terms, 2/10, n/30.

The information needed by the bookkeeper in recording each sale is obtained from a carbon copy of the sales invoice prepared by the billing clerk. As this invoice was entered in the sales record, a check mark was placed in the Check (√) column following the Accounts Receivable Dr. column to indicate that the invoice will be posted direct to the account of W. O. Davenport. The invoice was then posted to Mr. Davenport's account in the accounts receivable ledger, the amount of the merchandise sold, $232.96, being entered on one line and the amount of the federal excise tax, $12.94, being entered on the next line.

At the end of each day the total amount of any checks issued, the total amount of any deposits made during the day, and the bank balance at the end of the day are entered on the daily bank statement. Since this was the first day of May, the balance on April 30, amounting to $7,591.03, was brought forward to the top of a new page. The check issued on May 1, amounting to $300, was then entered on the daily bank statement and the new balance was extended.

Tuesday, May 2

Issued checks as follows:

No. 431, Standard Battery Co., $466.81, in payment of their invoice of April 24 for $481.25, less 3% discount.

No. 432, The Office Supply Co., $48.75, in full of account.

As these checks were entered in the record of checks drawn, check marks were placed in the Check (√) column following the amounts entered in the Accounts Payable Dr. column to indicate that the checks will be posted direct from the check stubs to the proper creditors' accounts in the accounts payable ledger. In posting to the account of the Standard Battery Co., the amount of the check, $466.81, was entered on one line and the amount of the discount, $14.44, was entered on the next line.

The total of the checks issued on May 2, amounting to $515.56, was entered on the daily bank statement and the balance was extended.

Wednesday, May 3

Received the following invoices:

The Cole Tire Co., Buffalo; tires and tubes, $368, federal excise tax, $36.40; terms, May 2 — 2/10, n/30; Big Four freight collect.

National Radio Mfg. Co., Philadelphia; radios, $167.50; terms, May 2 — 3/10, n/30; B. & O. freight collect.

Powers Printing Co., City; letterheads and envelopes, $23.25; terms, May 3 — n/30.

As these invoices were entered in the invoice record, check marks were placed in the Check (√) column following the Accounts Payable Cr. column to indicate that the invoices will be posted direct to the proper creditors' accounts in the accounts payable ledger. In posting the invoice received from The Cole Tire Co., the amount of the merchandise purchased, $368, was entered on one line and the amount of the federal excise tax, $36.40, was entered on the next line.

Thursday, May 4

Issued Check No. 433 for $674.61 to The Cole Tire Co. in payment of their invoice of April 25 for $687.40, less 2% discount.

Reference to the account of The Cole Tire Co. in the accounts payable ledger showed that on April 25 merchandise was purchased amounting to $639.28 on which the federal excise tax amounted to $48.12. The purchase price of the merchandise is subject to a discount of 2%, but of course the excise tax is not subject to discount. The amount of the check was computed as follows:

Merchandise purchased	$639.28
Less 2% discount	12.79
	$626.49
Plus federal excise tax	48.12
Net amount due	$674.61

In posting to the account of The Cole Tire Co., the amount of the check, $674.61, was entered on one line and the amount of the discount, $12.79, was entered on the next line.

Received the following invoices:

The Cole Tire Co., Buffalo; tires and tubes, $213.07, federal excise tax, $18.53; terms, May 3—2/10, n/30; shipped direct to Keiffer Garage, Kingston, freight collect.

Standard Battery Co., St. Louis; batteries, $180; terms, May 3—3/10, n/30; Big Four freight collect.

The Office Supply Co., City; office supplies, $26; terms, May 4—n/30.

Bryant & Wood are agents for The Cole Tire Co.; however, they do not necessarily carry in stock the entire line of tires and tubes. When an order is received for items that are not carried in stock, an order is placed with the company with instructions to ship direct to the customer, transportation charges collect. After the invoice was recorded in the invoice record and was posted to the account of The Cole Tire Co. in the accounts payable ledger, it was referred to the billing clerk with instructions to bill the Keiffer Garage.

Friday, May 5

Received a check for $448.41 from B. A. Fall in payment of merchandise sold him on April 26 amounting to $420.27, less 2% discount, plus federal excise tax, $36.55.

Made charge sales as follows:

No. 816, Service Tire Shop, City; tires, $172.65, federal excise tax, $13; terms, 2/10, n/30.

No. 817, C. J. Mead, Athens; tubes, $87.63, federal excise tax, $8.67; postage, 93 cents; terms, 2/10, n/30.

No. 818, Keiffer Garage, Kingston; tires, $319.79, federal excise tax, $27.81; terms, 2/10, n/30; shipped direct from factory, freight collect.

In entering Sales Invoice No. 817 in the sales record, the postage was charged to the customer's account and was credited to Postage Stamps, Account No. 174. In posting this invoice to the account of C. J. Mead in the accounts receivable ledger, the amount of the merchandise sold, $87.63, was entered on one line; the amount of the federal excise tax, $8.67, was entered on the next line; and the amount of the postage prepaid, 93 cents, was entered on the third line. The tires billed to the Keiffer Garage on Sales Invoice No. 818 are the ones that were shipped direct by The Cole Tire Co. on May 3 and for which an invoice was received on May 4.

Issued Check No. 434 for $697.53 to the National Radio Mfg. Co. in payment of their invoice of April 26 for $719.10, less 3% discount.

Saturday, May 6

Issued credit memorandum No. 24 to W. O. Davenport, $3.20, for one heavy-duty tube returned; tube, $2.88, federal excise tax, 32 cents.

The tube returned was billed on Sales Invoice No. 815. This transaction was recorded in the general journal, after which the credit memorandum was posted direct to the account of W. O. Davenport in the accounts receivable ledger, the credit for the tube, $2.88, being entered on one line and the credit for the tax, 32 cents, being entered on the next line.

Made the following cash sales:

No. 416, Grant Highway Garage, City; tires and tubes, $236.07, federal excise tax, $20.53.

No. 417, C. L. Nixon, Northumberland; tires, $145.36, federal excise tax, $10.94.

At the end of each day the carbon copies of the cash sales tickets are analyzed to ascertain the total sales by departments, after which an entry is made in the record of cash receipts debiting the Bank for the total amount of cash received and crediting Cash Sales by departments for the total sales made in each department and crediting Federal Excise Tax for the total tax.

Issued the following checks:

No. 435, $25, payable to Postage. (Cashed the check at the bank and purchased $25 worth of stamps.)

No. 436, Rubber Chain Co., $153.02, in payment of their invoice of April 27 for $157.75, less 3% discount.

No. 437, The Cole Tire Co., $197.59, in payment of merchandise purchased April 27 amounting to $183.14, less 2% discount, plus federal excise tax, $18.11.

END-OF-THE-WEEK WORK

(a) Footed the amount columns in all the books of original entry and proved the footings.

(b) Deposited $1,279.96 in the Liberty National Bank and entered the amount on the daily bank statement.

(c) Proved the bank balance in the following manner:

Balance, May 1	$7,591.03
Total receipts for the week ended May 6 per record of cash receipts	1,279.96
Total	$8,870.99
Less total checks issued during the week ended May 6 per record of checks drawn	2,563.31
Balance, May 6	$6,307.68

(d) Completed the individual posting from the books of original entry to the general ledger and the operating expense ledger accounts.

Monday, May 8

Issued credit memorandum No. 25 to Allegeron Dairy, $5, for two 6.00–16 tubes returned; tubes, $4.52, federal excise tax, 48 cents.

Received the following checks:

Wyatt & Son, $613.88, in payment of merchandise sold them April 28 amounting to $596, less 2% discount, plus federal excise tax, $29.80.

Allegeron Dairy, $349.10, in payment of merchandise sold April 10 for $321.25, plus federal excise tax, $27.85.

Made the following cash sales:

No. 418, R. L. Davids, Olean; batteries, $89.85; tires and tubes, $183.21, federal excise tax, $13.79; express collect.

No. 419, Kenton Garage, Kenton; tires, $90.95, federal excise tax, $6.85; called for.

Made petty cash disbursements as follows:

Typewriter repairs, $1.75. Voucher No. 56.

500 circular letters, $3.50. Voucher No. 57.

All disbursements from the petty cash fund are recorded in the petty cash disbursements record.

Issued charge-back invoice No. 15 to The Cole Tire Co., $34.46, for two 7.00–15 4-ply safety tires returned for credit; tires purchased April 29, $31.70, federal excise tax, $2.76.

This transaction was recorded in the general journal, after which the charge-back invoice was posted direct to the account of The Cole Tire Co. in the accounts payable ledger, the charge for the tires, $31.70, being entered on one line, and the charge for the tax, $2.76, being entered on the next line.

Issued the following checks:

No. 438, The Cole Tire Co., $290.62, in payment of balance due on merchandise purchased April 29 for $275.76, less 2% discount, plus federal excise tax, $20.38.

In computing the amount of the check to be issued it was necessary to refer to the account of The Cole Tire Co. and make the following calculations:

Merchandise purchased April 29		$307.46
Less merchandise returned for credit May 8		31.70
Amount subject to discount		$275.76
Discount @ 2%		5.52
		$270.24
Plus federal excise tax:		
Amount of tax charged on original purchase invoice	$23.14	
Less tax on tires returned May 8	2.76	20.38
Net amount due		$290.62

No. 439, National Radio Mfg. Co., $442.22, in payment of their invoice of April 28, $455.90, less 3% discount.

Tuesday, May 9

Received the following invoices:

Western Auto Supply Co., City; batteries, $21.50; terms, May 8 — 1/10, n/30; shipped to Union Garage, Uniontown, express collect.

The Cole Tire Co., Buffalo; tires and tubes, $517.96, federal excise tax, $45.04; terms, May 8 — 2/10, n/30; Big Four freight collect.

Office Equipment Co., City; calculating machine, $150; terms, May 9 — n/30.

Wednesday, May 10

Made charge sales as follows:

No. 819, Wade Garage, Gainesville; tires, $238.05, federal excise tax, $20.70; terms, 2/10, n/30; express collect.

No. 820, Courthouse Garage, Hamilton; radios and batteries, $362.80; tires, $200.38, federal excise tax, $17.42; terms, 2/10, n/30; express collect.

No. 821, B. A. Fall, Franklin; radio, $49.90; tires and tubes, $1,517.54, federal excise tax, $131.96; terms, 2/10, n/30; Pennsylvania freight collect.

No. 822, Union Garage, Uniontown; batteries, $26.50; terms, 2/10, n/30; shipped from factory, express collect.

The batteries billed to the Union Garage on Sales Invoice No. 822 are the ones that were shipped direct by the Western Auto Supply Co. on May 8 and for which an invoice was received on May 9.

Received a 30-day, 6% interest-bearing note (No. 164), dated May 9, for $750 from the Union Garage in temporary settlement of the balance due on their account May 1.

The note was recorded in the general journal and in the notes receivable register.

Issued credit memorandum No. 26 to the Service Tire Shop, $43.02, for two 7.00–15 4-ply tires returned; tires, $40.26, federal excise tax, $2.76. Inasmuch as the tires were defective, they were immediately returned to The Cole Tire Co. for credit at cost, $34.46, charge-back invoice No. 16, tires purchased May 3, $31.70, federal excise tax, $2.76.

It will be noted that the Service Tire Shop was given credit for the wholesale price of the tires while The Cole Tire Co. was charged for the manufacturer's price.

Issued Check No. 440 to The Daily Post for $12.50 in payment of an advertisement in the Sunday edition of May 7.

Thursday, May 11

Issued Check No. 441 for $127.01 to the Liberty National Bank to reimburse it for a dishonored check of the Four-Squares Garage, returned unpaid by the bank on which it was drawn with a notice stating the reason as "not sufficient funds."

The dishonored check was originally received in payment of sales invoice of April 19 for $129.60, less 2% discount. Bryant & Wood have arranged with the bank for all dishonored checks to be presented for reimbursement; hence when the dishonored check of the Four-Squares Garage was presented, Mr. Bryant issued Check No. 441 in settlement and wrote A. L. Jinks, President of the Four-Squares Garage, advising him that his check of April 28 had been returned unpaid and that it had been charged back to his account.

Received the following invoices:

Powers Printing Co., City; 5M price lists, $37.50; terms, May 11 — n/30.

The Cole Tire Co., Buffalo; tires and tubes, $698.62, federal excise tax, $52.58; terms, May 10 — 2/10, n/30; Big Four freight collect.

General Auto Supply Co., Akron; tires, $207.58, federal excise tax, $15.62; terms, May 10 — 3/10, n/30; shipped direct to B. A. Fall, Franklin, freight collect.

Johnson Paper Co., City; wrapping paper, $19.50; terms, May 11 — n/30.

Western Auto Supply Co., City; batteries, $19.95; terms, May 10 — 1/10, n/30; shipped to Bishop & Wells, Marysville; express collect.

Issued the following checks:

No. 442, The Cole Tire Co., $397.04, in payment of merchandise purchased May 2 for $368, less 2% discount, plus federal excise tax, $36.40.

No. 443, National Radio Mfg. Co., $162.47, in payment of their invoice of May 2 for $167.50, less 3% discount.

Received a check for $238.10 from W. O. Davenport in payment of balance due on merchandise sold him May 1; merchandise, $230.08, less 2% discount, plus federal excise tax, $12.62.

Friday, May 12

Discounted the Union Garage note (No. 164) for $750 at the Liberty National Bank at 6% and deposited the proceeds amounting to $750.36.

This note was received on May 10. Two lines were required to record the transaction in the record of cash receipts because of the credits required in the General Ledger column.

Made charge sales as follows:

No. 823, Bishop & Wells, Marysville; tires, $67.53, federal excise tax, $5.87; batteries, $26.50; postage, $1.08; terms, 2/10, n/30. (The batteries were shipped direct from the factory, express collect.)

No. 824, Hope Street Garage, City; radio and batteries, $88.55; tubes, $52.78, federal excise tax, $5.22; terms, 2/10, n/30.

No. 825, B. A. Fall, Franklin; tires, $308.02; federal excise tax, $26.78; terms, 2/10, n/30; shipped direct from factory, freight collect.

No. 826, Byers Tire Shop, City; tires and tubes, $1,838.12, federal excise tax, $159.83; terms, 2/10, n/30.

Received the following checks:

Xenia Transfer Co., $357.90, in payment of our invoice of April 29, $365.20, less 2% discount.

Watson Auto Repair Co., $425.50, in full of account.

Made the following cash sales:

No. 420, J. R. Downey, El Paso; radio, $34.20; called for.

No. 421, R. L. Rockwell, Live Oak; tires, $290.72, federal excise tax, $21.88; express collect.

Issued the following checks:

No. 444, The Cole Tire Co., $227.34, in payment of merchandise purchased May 3 for $213.07, less 2% discount, plus federal excise tax, $18.53.

No. 445, Standard Battery Co., $174.60, in payment of their invoice of May 3, $180, less 3% discount.

No. 446, Mays Heater Co., $48.51, in payment of their invoice of April 14, $49.50, less 2% discount.

Saturday, May 13

Issued Check No. 447 for $118.48 to the Moore Oil Co. in payment of gasoline and oil supplied during April.

Paid $3.50 out of the petty cash fund for repairs on truck. Voucher No. 58.

Sent a corrected invoice to the Wade Garage, Gainesville, for $78.35; covering five 6.00–16 4-ply safety tires at $14.55 each, plus federal excise tax, $1.12.

On Sales Invoice No. 805 dated April 25, the tires through an error were billed at $14.38 each, plus federal excise tax, $1.12.

In recording this transaction in the sales record, it was only necessary to debit Accounts Receivable and credit Sales, Dept. A, for 85 cents, which represented the increased amount of the corrected invoice.

END-OF-THE-WEEK WORK

(a) Footed the amount columns in all the books of original entry and the petty cash disbursements record and proved the footings.

(b) Deposited $2,715.93 in the Liberty National Bank.

(c) Proved the bank balance as follows:

Balance, May 1	$ 7,591.03
Total receipts for the period ended May 13 per record of cash receipts	4,746.25
Total	$12,337.28
Less total checks issued during period ended May 13 per record of checks drawn	4,564.10
Balance, May 13	$ 7,773.18

(d) Completed the individual posting from the books of original entry to the general ledger and the operating expense ledger accounts.

Monday, May 15

Made petty cash disbursements as follows:

Water bill, $2.75. Voucher No. 59.

1M shipping tags, $3.50. Voucher No. 60.

100 sheets carbon paper, $1.50. Voucher No. 61.

Painting window sign, $2.50. Voucher No. 62.

Made the following cash sales:

No. 422, E. R. Early, City; tires and tubes, $77.56, federal excise tax, $5.84.

No. 423, J. L. Minor, Quincy; radios and batteries, $131.40; express collect.

Received the following checks:

Service Tire Shop, $139.98 in payment of balance due on merchandise sold May 5; merchandise, $132.39, less 2% discount, plus federal excise tax, $10.24.

C. J. Mead, $171.48, in full of account, less 2% discount on merchandise sold him on May 5 amounting to $87.63, plus federal excise tax, $8.67, and postage, 93 cents.

Keiffer Garage, $341.20, in payment of merchandise sold on May 5 for $319.79, less 2% discount, plus federal excise tax, $27.81.

A. H. Day, $113.78, in full of account.

Central Garage, $269.42, to apply on account and a 60-day, 6% note (No. 165) for $500, dated May 15, in temporary settlement of the balance due.

After entering both the check and the note in the cash receipts record, they were posted immediately to the credit of the account of the Central Garage in the accounts receivable ledger. The amount of the check was entered on one line and the amount of the note on the next line.

Issued Check No. 448 for $206.40 to the Liberty National Bank, a U. S. depositary, in payment of the following taxes:

(a) Employees' income taxes (withheld during April)		$152.40
(b) Social security taxes imposed for old-age and survivors' insurance benefits —		
On employees (withheld during April)	$27.00	
On the employer	27.00	54.00
Total		$206.40

Issued Check No. 449 payable to Payroll for $1,191.30.

Bryant & Wood follow the policy of paying their employees on the fifteenth and the last day of each month. Inasmuch as they have more than eight employees, they are subject to the taxes imposed under the Federal Social Security Law for both old-age insurance benefits and for unemployment purposes. They are also required to make contributions to the state unemployment compensation fund. They are required to withhold a percentage of their employees' wages for both old-age insurance benefits and for income tax purposes. In addition to the wages paid to employees, the partnership agreement provides that each partner is to receive a salary of $400 a month, payable semimonthly. While the salaries of the partners constitute an operating expense of the business, they do not represent wages as defined in the social security and income tax laws and hence are not subject to the withholding provisions.

On each payday the bookkeeper is supplied with a report prepared by the payroll clerk showing the total amount of wages and salaries earned during the pay period, the amount of the payroll deductions, and the net amount of cash needed for payroll purposes. The report for May 15 appears at the top of page 493.

A check made payable to Payroll was issued for the net amount payable. This check was then cashed at the Liberty National Bank and currency and coins in the right denominations needed to pay each employee were obtained. The bookkeeper was instructed by Messrs. Bryant and Wood to deposit their salaries in their personal accounts and to furnish them with duplicate copies of the deposit tickets.

The waved lines appearing at this point in the books of original entry indicate omission of the transactions completed on the days between May 15 and 31.

PAYROLL STATEMENT FOR PERIOD ENDED MAY 15

Classification	Total Earnings	Deductions		Net Amount Payable
		O. A. B. Tax	Employees' Income Taxes	
Salaries of Store Clerks........	440.00	6.60	39.90	393.50
Wages of Truck Driver...........	100.00	1.50	3.20	95.30
Office Salaries.................	340.00	5.10	32.40	302.50
Partners' Salaries:				
J. A. Bryant....................	200.00	None	None	200.00
W. L. Wood......................	200.00	None	None	200.00
	1,280.00	13.20	75.50	1,191.30

Employer's payroll taxes:

(a) For old-age and survivors' insurance benefits @ 1½%..................		$13.20
(b) For unemployment compensation benefits—		
State @ 2.7%..	$23.76	
Federal (3% less state contributions of 2.7%).................	2.64	26.40
Total..		$39.60

Wednesday, May 31

Received the following invoices:

Western Auto Supply Co., City; battery, $12.80, express prepaid, $1.10; terms, May 31 — 1/10, n/30.

The Cole Tire Co., Buffalo; tires and tubes, $1,670.08, federal excise tax, $145.22; terms, May 29 — 2/10, n/30; Big Four freight collect.

Standard Battery Co., St. Louis; batteries, $518; terms, May 29 — 3/10, n/30; Big Four freight collect.

Office Equipment Co., City; one check writer, $35, less credit for exchange allowance on old check writer, $5; terms, May 29 — n/30.

The original cost of the old check writer was $25; but when it was traded in, the book value was only $5. This transaction was recorded in the invoice record by debiting Office Equipment, Account No. 23, for $35, the cost of the new check writer; by debiting Reserve for Depreciation of Office Equipment, Account No. 023, for $20, the amount of the reserve applicable to the old check writer; by crediting Office Equipment, Account No. 23, for $25, the original cost of the old check writer; and by crediting Accounts Payable for $30, the balance due the Office Equipment Co.

Received cashier's check for $300.75 from the Evanston Bank, Evanston, in payment of Peters Garage note (No. 161) for $300 plus interest $1.50, less collection charges 75 cents.

Louis F. Dolle, attorney at law, advises that he is unable to collect the $25 owed by G. A. Wheeler and Mr. Bryant has instructed that the account be charged off.

After recording this transaction in the general journal by debiting Reserve for Bad Debts, Account No. 013, and by crediting Accounts Receivable for $25, it was posted immediately as a credit to the account of G. A. Wheeler in the accounts receivable ledger.

Made charge sales as follows:

No. 850, W. M. Mason, City; radio, $37.95; terms, 2/10, n/30.

No. 851, Bond Service Station, Kingston; radio and batteries, $173.85; tires and tubes, $826.37, federal excise tax, $81.73; terms, 2/10, n/30; Pennsylvania freight collect.

No. 852, Courthouse Garage, Hamilton; radio and batteries, $73.70; tires and tubes, $450.86, federal excise tax, $33.94; terms, 2/10, n/30; shipped by prepaid express, $2.80.

It will be noted that the express prepaid on the merchandise sold to the Courthouse Garage at Hamilton was credited to Transportation Out, Account No. 719. Since this account is kept in the subsidiary operating expense ledger, it is also necessary to credit the freight to the general ledger control account for Operating Expenses, Account No. 71. The double posting is provided for by drawing a diagonal line through the Acct. No. column.

Paid $2.80 out of the petty cash fund for express charges on merchandise shipped to the Courthouse Garage, Hamilton. Voucher No. 67.

Bishop & Wells have advised that the tires and tubes shipped direct from the factory on May 24 arrived by express collect, $2.75, whereas a delivered price had been quoted them. Mr. Bryant, therefore, directed that a credit memorandum (No. 29) should be issued to Bishop & Wells for the amount of the express charges.

This transaction was recorded in the general journal by debiting Transportation Out, Account No. 719, in the Operating Expense column, and by crediting Accounts Receivable for $2.75. The credit memorandum was also posted direct to the account of Bishop & Wells in the accounts receivable ledger.

Paid $4.75 out of the petty cash fund to A. B. Roberts who returned an imperfect tube purchased for cash on May 23, $4.46, federal excise tax, 29 cents (Sale No. 426). Voucher No. 68. As instructed by Mr. Bryant, the tube was returned to The Cole Tire Co. and they were advised that we had charged their account for the cost price of the tube, $2.96, and the federal excise tax, 29 cents. Charge-back invoice No. 20.

In entering this transaction in the petty cash disbursements record, Sales Returns and Allowances, Dept. A, Account No. 0511, was charged for the selling price of the tube, $4.46, and Prepaid Federal Excise Tax, Account No. 176, was charged for the amount of the tax, 29 cents. An entry was also made in the general journal to record the value of the tube returned to The Cole Tire Co. In recording this transaction, Accounts Payable, Account No. 36, was debited for $3.25, Purchases Returns and Allowances, Dept. A, Account No. 061, was credited for $2.96 and Prepaid Federal Excise Tax, Account No. 176, was credited for 29 cents.

Issued the following checks:

No. 468, Citizens Garage, $20, in payment of May storage.

No. 469, Western Auto Supply Co., $20.79, in payment of their invoice of May 22, $21, less 1% discount.

No. 470, Hughes Transfer Co., $126.10, in payment of freight and drayage on incoming merchandise received during May.

According to Mr. Bryant's instructions, freight and drayage on incoming merchandise should be distributed on a basis of the value of the merchandise purchased for each department during the month. On this basis, Transportation In, Dept. A should be charged for $111.70 and Transportation In, Dept. B should be charged for $14.40.

Issued Check No. 471 payable to Payroll for $1,219.65.

PAYROLL STATEMENT FOR PERIOD ENDED MAY 31

Classification	Total Earnings	Deductions: O. A. B. Tax	Deductions: Employees' Income Taxes	Net Amount Payable
Salaries of Store Clerks	470.00	7.05	41.10	421.85
Wages of Truck Driver	100.00	1.50	3.20	95.30
Office Salaries	340.00	5.10	32.40	302.50
Partners' Salaries:				
J. A. Bryant	200.00	None	None	200.00
W. L. Wood	200.00	None	None	200.00
	1,310.00	13.65	76.70	1,219.65

Employer's payroll taxes:

(a) For old-age and survivors' insurance benefits @ 1½%		$13.65
(b) For unemployment compensation benefits—		
State @ 2.7%	$24.57	
Federal (3% less state contributions of 2.7%)	2.73	27.30
Total		$40.95

Issued Check No. 472 for $34.45 payable to Petty Cash to replenish the petty cash fund.

A statement of the petty cash disbursements for May, which is reproduced at the top of page 504, provides the information needed in recording the check in the record of checks drawn.

(Continued on page 504)

INVOICE RECORD FOR MONTH OF *May* 19--

Debits: Purchases Dept. A	Debits: Purchases Dept. B	Debits: Federal Excise Tax	Debits: General Ledger Acct. No.	Debits: General Ledger Amount	√	Day	Date of Inv.	Inv. No.	Name	Credits: Accounts Payable	√	Credits: General Ledger Acct. No.	Credits: General Ledger Amount	√
									AMOUNTS FORWARDED					
368 00		36 40				3	5/2	91	The Cole Tire Co.	404 40	√			
	167 50					3	5/2	92	National Radio Mfg. Co.	167 50	√			
			173	23 25	√	3	5/3	93	Powers Printing Co.	23 25	√			
213 07		18 53				4	5/3	94	The Cole Tire Co.	231 60	√			
	180 00					4	5/3	95	Standard Battery Co.	180 00	√			
			173	26 00	√	4	5/4	96	The Office Supply Co.	26 00	√			
581 07	347 50	54 93		49 25						1032 75				
	21 50					9	5/8	97	Western Auto Sup. Co.	21 50	√			
517 96		45 04				9	5/8	98	The Cole Tire Co.	563 00	√			
			23	150 00	√	9	5/9	99	Office Equipment Co.	150 00	√			
			172	37 50	√	11	5/11	100	Powers Printing Co.	37 50	√			
698 62		52 58				11	5/10	101	The Cole Tire Co.	751 20	√			
207 58		15 62				11	5/10	102	General Auto Sup. Co.	223 20	√			
			171	19 50	√	11	5/11	103	Johnson Paper Co.	19 50	√			
	19 95					11	5/10	104	Western Auto Sup. Co.	19 95	√			
2005 23	388 95	168 17		256 25						2818 60				
	12 80		64	1 10	√	31	5/31	118	Western Auto Sup. Co.	13 90	√			
1670 08		145 22				31	5/29	119	The Cole Tire Co.	1815 30	√			
	518 00					31	5/29	120	Standard Battery Co.	518 00	√			
			23	35 00	√	31	5/29	121	Office Equipment Co.	30 00	√	23	25 00	√
			023	20 00	√									
8546 28	1197 85	683 70		469 50						10872 33			25 00	
8546 28	1197 85	683 70		469 50						10872 33			25 00	
(61)	(62)	(176)		(√)						(36)			(√)	

SALES RECORD FOR MONTH OF *May* 19--

DEBITS								CREDITS					
General Ledger			Accounts Receivable	√	Day	Name	Sale No.	Sales		Federal Excise Tax	General Ledger		
Acct. No.	Amount	√						Dept. A	Dept. B		Acct. No.	Amount	√
						AMOUNTS FORWARDED							
			245 90	√	1	W. O. Davenport	815	148 76	84 20	12 94			
			185 65	√	5	Service Tire Shop	816	172 65		13 00			
			97 23	√	5	C. J. Mead	817	87 63		8 67	174	93	√
			347 60	√	5	Kieffer Garage	818	319 79		27 81			
			876 38					728 83	84 20	62 42		93	
			258 75	√	10	Wade Garage	819	238 05		20 70			
			580 60	√	10	Courthouse Garage	820	200 38	362 80	17 42			
			1699 40	√	10	B. A. Fall	821	1517 54	49 90	131 96			
			26 50	√	10	Union Garage	822		26 50				
			100 98	√	12	Bishop & Wells	823	67 53	26 50	5 87	174	1 08	√
			146 55	√	12	Hope St. Garage	824	52 78	88 55	5 22			
			334 80	√	12	B. A. Fall	825	308 02		26 78			
			1997 95	√	12	Byers Tire Shop	826	1838 12		159 83			
			85	√	13	Wade Garage	805	85					
			6022 76					4952 10	638 45	430 20		2 01	
			37 95	√	31	W. M. Mason	850		37 95				
			1081 95	√	31	Bond Service Station	851	826 37	173 85	81 73			
			561 30	√	31	Courthouse Garage	852	450 86	73 70	33 94	71/719	2 80	√
			13687 35					10555 09	2074 20	844 41		213 65	
			13687 35					10555 09	2074 20	844 41		213 65	
			(132)					(511)	(512)	(176)		(√)	

RECORD OF CASH RECEIPTS FOR MONTH OF *May* 19--

DEBITS							CREDITS							
General Ledger									Cash Sales		General Ledger			
Acct. No.	Amount	√	Sales Discount	Bank Net Amount	Day	Received From—Description	Accounts Receivable	√	Dept. A	Dept. B	Acct. No.	Amount	√
						AMOUNTS FORWARDED							
			7 85	418 65	1	*W. O. Davenport*	426 50	√					
			8 41	448 41	5	*B. A. Fall*	456 82	√					
				412 90	6	*Cash Sales*			381 43		176	31 47	√
			16 26	1279 96			883 32		381 43			31 47	
			11 92	613 88	8	*Wyatt & Son*	625 80	√					
				349 10	8	*Allegeron Dairy*	349 10	√					
				384 65	8	*Cash Sales*			274 16	89 85	176	20 64	√
			4 60	238 10	11	*W. O. Davenport*	242 70	√					
				750 36	12	*Bank — Note #164 disc.*					131	750 00	√
						Interest Income					522	36	√
			7 30	357 90	12	*Xenia Transfer Co.*	365 20	√					
				425 50	12	*Watson Auto Repair Co.*	425 50	√					
				346 80	12	*Cash Sales*			290 72	34 20	176	21 88	√
			40 08	4746 25			2891 62		946 31	124 05		824 35	
				214 80	15	*Cash Sales*			77 56	131 40	176	5 84	√
			2 65	139 98	15	*Service Tire Shop*	142 63	√					
			1 75	171 48	15	*C. J. Mead*	173 23	√					
			6 40	341 20	15	*Kieffer Garage*	347 60	√					
				113 78	15	*A. H. Day*	113 78	√					
131	500 00	√		269 42	15	*Central Garage—Note #165*	769 42	√					
754	75	√		300 75	31	*Evanston Bk. — Note #161*					131	300 00	√
						Interest Income					522	1 50	√
	1400 72		265 18	12353 39			11099 88		1351 48	398 55		1169 38	
	1400 72		265 18	12353 39			11099 88		1351 48	398 55		1169 38	
	(√)		(751)	(111)			(132)		(511)	(512)		(√)	

RECORD OF CHECKS DRAWN FOR MONTH OF *May* 19--

DEBITS: General Ledger Acct. No.	General Ledger Amount	√	Operating Expenses Acct. No.	Operating Expenses Amount	√	Accounts Payable	√	Day	Drawn to the Order of	CREDITS: General Ledger Acct. No.	General Ledger Amount	√	Purchases Discount	Check No.	Bank Net Amount
									AMOUNTS FORWARDED						
			731	300 00	√			1	H. H. Davids					430	300 00
						481 25	√	2	Standard Battery Co.				14 44	431	466 81
						48 75	√	2	The Office Sup. Co.					432	48 75
						687 40	√	4	The Cole Tire Co.				12 79	433	674 61
						719 10	√	5	Nat. Radio Mfg. Co.				21 57	434	697 53
174	25 00	√						6	Postage					435	25 00
						157 75	√	6	Rubber Chain Co.				4 73	436	153 02
						201 25	√	6	The Cole Tire Co.				3 66	437	197 59
	25 00			300 00		2205 50							57 10		2563 31
						296 14	√	8	The Cole Tire Co.				5 52	438	290 62
						455 90	√	8	Nat. Radio Mfg. Co.				13 68	439	442 22
			711	12 50	√			10	Daily Post					440	12 50
132	129 60	√						11	Liberty Nat. Bank	751	2 59	√		441	127 01
						404 40	√	11	The Cole Tire Co.				7 36	442	397 04
						167 50	√	11	Nat. Radio Mfg. Co.				5 03	443	162 47
						231 60	√	12	The Cole Tire Co.				4 26	444	227 34
						180 00	√	12	Standard Battery Co.				5 40	445	174 60
						49 50	√	12	Mays Heater Co.				99	446	48 51
			716	118 48	√			13	Moore Oil Co.					447	118 48
	154 60			430 98		4080 54					2 59		99 43		4564 10
34	152 40	√						15	Liberty Nat. Bank					448	206 40
31	54 00	√													
			712	440 00	√			15	Payroll	31	26 40	√		449	1191 30
			713	100 00	√					32	2 64	√			
			733	340 00	√					33	23 76	√			
			714	200 00	√					34	75 50	√			
			732	200 00	√										
			742	15 84	√										
			743	23 76	√										
	361 00			1750 58		4080 54					130 89		99 43		5961 80
	361 00			1750 58		4080 54		15	Amounts Forwarded		130 89		99 43		5961 80

RECORD OF CHECKS DRAWN FOR MONTH OF *May* 19--

DEBITS										CREDITS					
General Ledger			Operating Expenses			Accounts Payable	√	Day	Drawn to the Order of	General Ledger			Purchases Discount	Check No.	Bank Net Amount
Acct. No.	Amount	√	Acct. No.	Amount	√					Acct. No.	Amount	√			
	361 00			1750 58		4080 54		15	AMOUNTS FORWARDED		130 89		99 43		5961 80
			718	20 00	√			31	*Citizens Garage*					468	20 00
						21 00	√	31	*Western Auto Sup. Co.*				21	469	20 79
63	111 70	√						31	*Hughes Transfer Co.*					470	126 10
64	14 40	√													
			712	470 00	√			31	*Payroll*	31	27 30	√		471	1219 65
			713	100 00	√					32	2 73	√			
			733	340 00	√					33	24 57	√			
			714	200 00	√					34	76 70	√			
			732	200 00	√										
			742	16 38	√										
			743	24 57	√										
63	1 00	√	711	3 50	√			31	*Petty Cash Fund*					472	34 45
173	1 50	√	717	3 50	√										
0511	4 46	√	719	4 80	√										
176	29	√	727	7 25	√										
			734	2 75	√										
			735	1 15	√										
			744	4 25	√										
	726 85			2988 48		9266 56					262 19		243 13		12476 57
	726 85			2988 48		9266 56					262 19		243 13		12476 57
	(√)			(71)		(36)					(√)		(521)		(111)

GENERAL JOURNAL FOR MONTH OF *May* 19--

Debits: Operating Expenses Acct. No.	Operating Expenses Amount	√	Accounts Payable	√	General Ledger Acct. No.	General Ledger Amount	√	Day	Description	Credits: General Ledger Acct. No.	General Ledger Amount	√	Accounts Payable	√	Accounts Receivable	√
									AMOUNTS FORWARDED							
					0511	2 88	√	6	W. O. Davenport —						3 20	√
					176	32	√		C M 24							
						3 20									3 20	
					0511	4 52	√	8	Allegeron Dairy —						5 00	√
					176	48	√		C M 25							
			34 46	√				8	The Cole Tire Co. —	061	31 70	√				
									C B 15	176	2 76	√				
					131	750 00	√	10	Union Garage—N 164						750 00	√
					0511	40 26	√	10	Service Tire Shop —						43 02	√
					176	2 76	√		C M 26							
			34 46	√				10	The Cole Tire Co. —	061	31 70	√				
									C B 16	176	2 76	√				
			68 92			801 22					68 92				801 22	
					013	25 00	√	31	G. A. Wheeler						25 00	√
719	2 75	√						31	Bishop & Wells CM 29						2 75	√
			3 25	√				31	The Cole Tire Co. —	061	2 96	√				
									C B 20	176	29	√				
	2 75		72 17			1560 27					72 17				1563 02	
	2 75		72 17			1560 27					72 17				1563 02	
	(71)		(36)			(√)					(√)				(132)	

PETTY CASH DISBURSEMENTS FOR MONTH OF *May* 19--

Day	Description	Vou. No.	Total Amount	Distribution of Charges: 711	717	719	727	734	735	744	Account	Amount
1	BROUGHT FORWARD $50.00											
8	*Typewriter repairs*	56	1 75							1 75		
8	*Circular letters*	57	3 50	3 50								
13	*Repairs on truck*	58	3 50		3 50							
			8 75	3 50	3 50					1 75		
15	*Water bill*	59	2 75					2 75				
15	*Shipping tags*	60	3 50				3 50					
15	*Carbon paper*	61	1 50								173	1 50
15	*Painting window sign*	62	2 50							2 50		
			19 00	3 50	3 50		3 50	2 75		4 25		1 50
31	*Express charges*	67	2 80			2 80						
31	*Returns, A. B. Roberts*	68	4 75								0511	4 46
											176	29
			34 45	3 50	3 50	4 80	7 25	2 75	1 15	4 25		7 25
			34 45	3 50	3 50	4 80	7 25	2 75	1 15	4 25		7 25
31	*Balance* $15.55											
	Rec'd in fund 34.45											
	Total $50.00											

DAILY STATEMENT OF LIBERTY NATIONAL BANK FOR MONTH OF *May* 19--

Outstanding Checks			Memorandum	Daily Bank Balance			
Check No.	Amount	√		Day	Deposits	Checks	Balance
			BALANCE PREVIOUS MONTH				7591 03
				1		300 00	7291 03
				2		515 56	6775 47
				3			
				4		674 61	6100 86
				5		697 53	5403 33
				6	1279 96	375 61	6307 68
				7			
				8		732 84	5574 84
				9			
				10		12 50	5562 34
				11		686 52	4875 82
				12	750 36	450 45	5175 73
				13	2715 93	118 48	7773 18
				14			
				15		1397 70	6375 48
Total Checks Outstanding				30			
Our Balance				31	1086 55	1420 99	7467 85
Bank Balance			Totals		12353 39	12476 57	

STATEMENT OF PETTY CASH DISBURSEMENTS FOR MAY

Acct. No.	Title	Amount
173	Office Supplies	$ 1.50
176	Prepaid Federal Excise Tax	.29
0511	Sales Returns and Allowances, Dept. A	4.46
63	Transportation In, Dept. A	1.00
711	Advertising Expense	3.50
717	Repairs on Truck	3.50
719	Transportation Out	4.80
727	Miscellaneous Selling Expense	7.25
734	Light and Water	2.75
735	Telephone and Telegrams	1.15
744	Miscellaneous General Expense	4.25
	Total Disbursements	$34.45

END-OF-THE-MONTH WORK

(a) Footed the amount columns, proved the footings, entered the totals, and ruled each of the books of original entry and the petty cash disbursements record.

(b) Deposited $1,086.55 in the Liberty National Bank.

(c) Proved the bank balance as follows:

Balance, May 1	$ 7,591.03
Total receipts for the month ended May 31 per record of cash receipts	12,353.39
Total	$19,944.42
Less total checks issued during month ended May 31 per record of checks drawn	12,476.57
Balance, May 31	$ 7,467.85

(d) Completed the individual posting from the books of original entry to the general ledger and the operating expense ledger accounts.

(e) Completed the summary posting of the columnar totals of each of the books of original entry to the general ledger accounts.

PRACTICE ASSIGNMENT No. 36. The workbook contains an analysis test that should be completed at this time. Before beginning work on the test, this unit should be studied thoroughly. The narrative of transactions for May should be checked with the illustrations to see how each transaction is recorded and to note the effect of each transaction on the accounts involved. Special attention should be given to the analyses following certain transactions. Unless the procedure involved in recording the transactions completed by Bryant & Wood during the month of May is thoroughly understood, you cannot hope to make a satisfactory grade on the test.

Unit Eighteen

ADJUSTING ENTRIES AND THE WORK SHEET

XXXVII ADJUSTING THE OPERATING EXPENSE ACCOUNTS

Periodically, the accountant should prepare financial statements and such schedules as are considered essential to sound business management. A balance sheet and a profit and loss statement are the basic financial statements included in an annual report. Much additional information may be provided by means of supporting schedules covering accounts receivable, accounts payable, operating expenses, cost of sales, and other accounting or statistical data.

In addition to an annual report, many firms require their accountants to prepare monthly reports setting forth the financial condition of the enterprise at the end of each month and the results of operations during each month. Such information provided monthly should be a distinct aid in the conduct of a business. To wait until the end of the year to interpret the accounts and to ascertain (a) the financial condition of the business and (b) the results of current operations may lead to serious consequences. Financial statements may be prepared at the end of each fiscal period; the fiscal period may be a year or any part of a year. Financial reports may thus be prepared on a monthly, quarterly, semiannual, or annual basis. In Part I of this course the procedure in preparing annual statements was treated in detail. In this unit the procedure in adjusting and classifying the accounts preliminary to the preparation of monthly reports is developed.

When the operating expense accounts are kept in a subsidiary ledger with a control account in the general ledger, it is usually necessary to adjust certain accounts at the end of each month in order that the true results of operations will be reflected. The need for adjusting certain operating expense accounts monthly arises from several factors. Certain assets depreciate continually, while other assets are consumed in the operation of a business. Depreciation is an expense that increases the cost of doing business. Supplies that are consumed in operating a business add to the cost of doing business. Prepaid insurance expires with the lapse of time and thus becomes an expense. Certain expenses may accrue and if the amount accrued is not recorded at the end of each month, the expense accounts will not reflect currently the true cost of operating an enterprise. Provision should also be made for the amount of bad debt losses anticipated. When such provision is made under the reserve method, the amount added to the reserve each month is recorded as a loss at the time of setting up the reserve.

The accounts of Bryant & Wood will be used to illustrate the procedure in adjusting the operating expense accounts monthly. The books of original entry, providing a record of some of the transactions completed during the month of May, are reproduced in the preceding unit. The following data provide the information needed in adjusting the operating expense accounts at the end of May:

BRYANT & WOOD

DATA FOR ADJUSTING THE OPERATING EXPENSE ACCOUNTS

May 31, 19--

Depreciation of Store Equipment, 10%		$12.50
Depreciation of Delivery Equipment, 25%		26.04
Depreciation of Office Equipment, 10%		20.83
Store Supplies Consumed during month		92.75
Advertising Supplies Consumed during month		28.35
Office Supplies Consumed during month		57.35
Postage Stamps Consumed during month:		
Selling Expense	$15.32	
Administration Expense	15.33	30.65
Insurance Expired during month:		
On Merchandise	$15.00	
On Delivery Equipment	12.50	
On Store Equipment	1.25	
On Office Equipment	2.50	31.25
Increase in Accrued Property Taxes Payable at end of month		30.00
Provision for Bad Debts, ½% of charge sales for May		68.44

Journalizing the Adjusting Entries. The entries required to adjust the operating expense accounts may be made on the work sheet in the manner illustrated in Unit Seven of this textbook or they may be journalized and posted to the accounts prior to making a work sheet. Bryant & Wood follow the latter practice. The adjusting entries required at the end of May are shown recorded in the general journal reproduced on page 507. By providing a special Dr. column in the general journal for

GENERAL JOURNAL FOR MONTH OF MAY, 19--

Debits									Credits				
Operating Expenses			Accounts Payable	General Ledger			Day	Description	General Ledger			Accounts Payable	Accounts Receivable
Acct. No.	Amount	√		Acct. No.	Amount	√			Acct. No.	Amount	√		
								Amounts Forwarded					
							31	Adjusting Entries:					
725	12 50	√						Depr. of store equipment	021	12 50	√		
726	26 04	√						Depr. of delivery equipment	022	26 04	√		
741	20 83	√						Depr. of office equipment	023	20 83	√		
723	92 75	√						Store supplies consumed	171	92 75	√		
711	28 35	√						Advertising supplies consumed	172	28 35	√		
738	57 35	√						Office supplies consumed	173	57 35	√		
724	15 32	√						Postage stamps consumed	174	30 65	√		
739	15 33	√											
720	15 00	√						Insurance expired	175	31 25	√		
721	12 50	√											
722	1 25	√											
740	2 50	√											
737	30 00	√						Accrued property taxes	38	30 00	√		
736	68 44	√						Provision for bad debts	013	68 44	√		
	398 16									*398 16*			
	398 16									398 16			
	-71-									-√-			

Operating Expense Adjustments

recording operating expenses, summary posting of the monthly total to the debit of the operating expense control account in the general ledger is made possible.

Depreciation Expense. Bryant & Wood use the group method of accounting for fixed assets, separate accounts being kept in the general ledger for store equipment, delivery equipment, and office equipment. The assets charged to each of these accounts have approximately the same average useful life. In computing the amount of depreciation sustained each month, the basis is the cost of the assets owned at the beginning of the month. Depreciation is not considered on assets owned less than a month. The factors involved in ascertaining the amount of depreciation sustained during May are shown in the following schedule:

SCHEDULE OF DEPRECIATION SUSTAINED DURING MAY

Fixed Assets	Cost	Annual Rate of Depreciation	Depreciation Sustained During Month
Store Equipment	$1,500	10%	$12.50
Delivery Equipment	1,250	25%	26.04
Office Equipment	2,500	10%	20.83
Total depreciation sustained during month........			$59.37

Bryant & Wood keep separate depreciation expense accounts and reserve accounts for each group of fixed assets. These accounts are as follows:

725 Depreciation of Store Equipment
726 Depreciation of Delivery Equipment
741 Depreciation of Office Equipment
021 Reserve for Depreciation of Store Equipment
022 Reserve for Depreciation of Delivery Equipment
023 Reserve for Depreciation of Office Equipment

Keeping separate expense accounts for the depreciation sustained on different groups of fixed assets facilitates a proper classification of the expenses in the monthly and annual reports. The depreciation on each group of fixed assets is recorded by debiting the proper depreciation expense account and by crediting the proper reserve account.

Supplies Consumed. Supplies of all kinds, including store supplies, advertising supplies, office supplies, and postage stamps, constitute assets when purchased but become expenses when consumed. Instead of charging such supplies to expense at the time of purchase, they are recorded as assets and adjustments are made at the end of each month for the amounts consumed during the month in the operations of the business. The factors involved in ascertaining the amount of supplies consumed by Bryant & Wood during May are shown in the following schedule:

SCHEDULE OF SUPPLIES CONSUMED DURING MAY

Supplies	Account Balance End of Month	Amount on Hand End of Month Per Stock Records	Amount Consumed During Month
Store Supplies	$154.00	$61.25	$ 92.75
Advertising Supplies	93.55	65.20	28.35
Office Supplies	105.95	48.60	57.35
Postage Stamps	39.45	8.80	30.65
Total supplies consumed during month			$209.10

Bryant & Wood keep separate expense accounts for each kind of supplies consumed. These accounts are as follows:

723 Store Supplies Consumed
711 Advertising Expense
738 Office Supplies Consumed
724 Postage (Selling)
739 Postage (Administration)

Keeping separate expense accounts for supplies consumed facilitates a proper classification of the expenses in the monthly and annual reports. The amount of each kind of supplies consumed during the month is recorded by debiting the proper operating expense account and by crediting the proper asset account. Of the total amount of postage stamps used during the month, one half was used in selling and the other half in administration. The amount used in selling was charged to Account No. 724 and the amount used in administration was charged to Account No. 739, while the total amount of stamps consumed was credited to Account No. 174.

Insurance Expired. Prepaid insurance premiums are usually recorded in the same manner as supplies. At the time of paying a premium, the amount paid is recorded as an asset; then at the end of each month the insurance expired during the month is recorded as an expense. Bryant & Wood keep separate expense accounts for the insurance expired on different kinds of property. These accounts are as follows:

720 Expired Insurance on Merchandise
721 Expired Insurance on Delivery Equipment
722 Expired Insurance on Store Equipment
740 Expired Insurance on Office Equipment

The information needed in ascertaining the amount of insurance expired on each kind of property owned was obtained from their insurance policy register. The factors involved are shown in the following schedule:

SCHEDULE OF INSURANCE EXPIRED DURING MAY

Policy Number	Property Insured	Premium Paid	Term of Policy	Amount Expired During Month
664218	Merchandise	$45.00	One Year	$ 3.75
92368	Merchandise	45.00	One Year	3.75
372085	Merchandise	45.00	One Year	3.75
13926B	Merchandise	45.00	One Year	3.75
16431A	Delivery Equipment	15.00	One Year	1.25
67231	Delivery Equipment	45.00	One Year	3.75
62981	Delivery Equipment	90.00	One Year	7.50
369810	Store Equipment	15.00	One Year	1.25
391042	Office Equipment	30.00	One Year	2.50
Total amount of insurance expired during month.......				$31.25

The insurance expired on each kind of property is recorded by debiting the respective expense accounts for the proper amounts and by crediting Prepaid Insurance, Account No. 175, for the total amount of insurance expired.

Accrued Expenses. When it is the policy of a firm to make monthly adjustment of the operating expense accounts, it will be necessary to make adjustment for any increases or any decreases in the amounts accrued at the end of each month. Rent, wages, property taxes, and other operating expenses may accrue. For example, where wages are paid weekly, there will be a certain amount accrued at the end of any month in which the wages earned are not paid in full on the last day of the month. To determine the amount of the required adjustment, it is necessary to compute the amount of wages actually accrued on the last day of the month and to compare this amount with the balance of the account with Accrued Wages Payable. Should there be an increase of $200 in the amount of wages accrued at the end of a particular month, an adjusting entry should be made debiting Wages and crediting Accrued Wages Payable for $200. On the other hand, if there should be a decrease of $200 in the amount of wages accrued at the end of a particular month, it would be necessary to make an adjusting entry debiting Accrued Wages Payable and crediting Wages for $200. It will be seen that any adjustment in accrued wages payable also affects the operating expense account with wages.

An analysis of the accounts kept by Bryant & Wood revealed that the only expense accrued at the end of May was property taxes. Under the laws of the state in which the firm is located, a tax is imposed on personal property, including the merchandise and equipment owned. The tax is payable semiannually, the first half being payable on December 20 and the last half on June 20 of the ensuing year. Since Bryant & Wood follow the practice of preparing monthly reports of operating expenses, the amount of the tax is estimated at the beginning of the year and an adjusting entry is made at the end of each month to record the amount accrued during the month. The estimated amount of such taxes for the current year is $360; hence the amount to be recorded each month is $30. The accrued taxes for May were recorded by debiting Property Taxes, Account No. 737, and by crediting Accrued Property Taxes Payable, Account No. 38.

Bad Debts. Bryant & Wood use the reserve method in accounting for bad debts. By reference to the sales record at the end of each month, the accountant ascertains the amount of the charge sales for the month and multiplies this amount by ½ per cent. For the month of May the total charge sales amounted to $13,687.35. One half per cent of this amount is $68.44. This was recorded by debiting Loss on Bad Debts, Account No. 736, and by crediting Reserve for Bad Debts, Account No. 013.

Posting the Adjusting Entries. The adjusting entries should be posted in the usual manner. This involves both individual posting and summary posting. In completing the individual posting, each item entered in the Operating Expenses Dr. column should be posted to the proper account in the operating expense ledger and each item entered in the General Ledger Cr. column should be posted to the proper account in the general ledger. As each item is posted, a check mark should be placed in the Check (√) column of the general journal immediately following the amount posted. The number of the general journal page from which the item is posted should also be entered in the Folio column of the proper ledger immediately preceding the amount posted.

In completing the summary posting, the total of the Operating Expenses Dr. column should be posted to the debit of the operating expense control account in the general ledger. For cross-reference purposes, the number of the operating expense control account should be entered in the general journal immediately below the amount posted, and the number of the general journal page from which the amount is posted should be entered in the Folio column of the general ledger immediately preceding the amount posted. The total of the General Ledger Cr. column need not be posted, as each item entered in this column has already been posted to the proper general ledger account. After completing the posting at the end of May, the operating expense control account in the general ledger appeared as follows:

OPERATING EXPENSES — Account No. 71

Date		Item	Ref.	Amount	Date		Item	Ref.	Amount
19--					19--				
May	1	Balance	√	36,197.34	May	27		S 497	2.00
	31		CD 500	2,988.48		31		S 497	2.80
	31		GJ 501	2.75					*4.80*
	31		GJ 507	398.16					
		39,581.93		*39,586.73*					

Trial Balance. After the individual and summary posting for May was completed, a trial balance of the general ledger accounts was taken. The trial balance is reproduced on page 513.

Schedules. Following the preparation of a trial balance, it is customary to prepare schedules of the account balances in each of the subsidiary ledgers as a means of proving the control account balances. Bryant & Wood keep three subsidiary ledgers, including an accounts receivable ledger, an accounts payable ledger, and an operating expense ledger. The schedule of accounts receivable is reproduced below and the schedules of accounts payable and operating expenses are reproduced on page 514.

BRYANT & WOOD
SCHEDULE OF ACCOUNTS RECEIVABLE
May 31, 19—

Bayless Bros	$ 314.60
Bishop & Wells	199.83
Bond Service Station	1,081.95
Byers Tire Shop	273.35
Central Garage	255.35
Courthouse Garage	616.85
W. O. Davenport	370.00
A. H. Day	196.77
B. A. Fall	334.80
General Supply Co	47.05
Hardin Farm	254.00
Hoole Tire Co	12.20
B. C. Jenkins & Son	176.45
Lincoln Garage	27.30
Lincoln Highway Tire Shop	161.17
W. M. Mason	37.95
Peters Garage	325.00
Porter & Wells	1,232.50
Service Tire Shop	313.85
W. D. Trotter	295.90
Union Garage	26.50
Wyatt & Son	118.50
	$6,671.87

BRYANT & WOOD

TRIAL BALANCE, MAY 31, 19--

Accounts	Nos.	Dr. Balances	Cr. Balances
Liberty National Bank	111	$ 7,467.85	
Petty Cash Fund	112	50.00	
U. S. Treasury Bonds	12	9,900.00	
Notes Receivable	131	3,203.36	
Accounts Receivable	132	6,671.87	
Reserve for Bad Debts	013		$ 455.94
Merchandise Inventory, Dept. A	14	21,847.90	
Merchandise Inventory, Dept. B	15	3,121.13	
Accrued Interest Receivable	16	10.00	
Store Supplies	171	61.25	
Advertising Supplies	172	65.20	
Office Supplies	173	48.60	
Postage Stamps	174	8.80	
Prepaid Insurance	175	168.75	
Prepaid Federal Excise Tax	176	2,454.29	
Store Equipment	21	1,543.50	
Res. for Depr. of Store Equipment	021		332.50
Delivery Equipment	22	1,250.00	
Res. for Depr. of Delivery Equipment	022		476.04
Office Equipment	23	2,660.00	
Res. for Depr. of Office Equipment	023		400.83
Federal Old-Age Insurance Taxes Payable	31		53.70
Federal Unemployment Taxes Payable	32		66.54
State Unemployment Contributions Payable	33		90.70
Employees' Income Taxes Payable	34		152.20
Notes Payable	35		3,500.00
Accounts Payable	36		4,790.10
Accrued Interest Payable	37		22.50
Accrued Property Taxes Payable	38		180.00
J. A. Bryant, Partner	41		27,000.00
J. A. Bryant, Drawing	411	725.43	
W. L. Wood, Partner	42		27,000.00
W. L. Wood, Drawing	421	436.62	
Sales, Dept. A	511		102,634.44
Sales Returns & Allowances, Dept. A	0511	1,612.40	
Sales, Dept. B	512		19,585.00
Sales Returns & Allowances, Dept. B	0512	75.00	
Purchases Discount	521		1,669.38
Interest Income	522		129.38
Purchases, Dept. A	61	72,657.43	
Purchases Returns & Allowances, Dept. A	061		652.00
Purchases, Dept. B	62	10,250.85	
Purchases Returns & Allowances, Dept. B	062		36.35
Transportation In, Dept. A	63	1,220.70	
Transportation In, Dept. B	64	175.60	
Operating Expenses	71	39,581.93	
Sales Discount	751	1,365.33	
Interest Expense	752	194.37	
Charitable Contributions	753	370.48	
Collection Expense	754	28.96	
		$189,227.60	$189,227.60

BRYANT & WOOD

SCHEDULE OF ACCOUNTS PAYABLE

May 31, 19—

Bannister Mfg. Co	$ 43.50
The Cole Tire Co	3,861.65
Jackson Box Co	7.50
Johnson Paper Co	60.00
Office Equipment Co	180.00
The Office Supply Co	31.20
Powers Printing Co	60.75
Standard Battery Co	518.00
Western Auto Supply Co	27.50
	$4,790.10

BRYANT & WOOD

SCHEDULE OF OPERATING EXPENSES

FOR THE ELEVEN-MONTHS' PERIOD ENDED MAY 31, 19--

Accounts	Nos.	
Advertising Expense	711	$ 1,112.85
Salaries of Store Clerks	712	9,497.00
Wages of Truck Driver	713	1,950.00
W. L. Wood, Salary	714	4,400.00
W. L. Wood, Traveling Expense	715	612.50
Gas and Oil for Truck	716	784.48
Repairs on Truck	717	130.25
Garage Rent	718	220.00
Transportation Out	719	30.25
Expired Insurance on Merchandise	720	165.00
Expired Insurance on Delivery Equipment	721	137.50
Expired Insurance on Store Equipment	722	13.75
Store Supplies Consumed	723	845.10
Postage	724	481.12
Depr. of Store Equipment	725	137.50
Depr. of Delivery Equipment	726	286.46
Misc. Selling Expense	727	138.90
Rent	731	3,300.00
J. A. Bryant, Salary	732	4,400.00
Office Salaries	733	7,400.00
Light and Water	734	82.65
Telephone and Telegrams	735	157.01
Loss on Bad Debts	736	660.94
Property Taxes	737	330.00
Office Supplies Consumed	738	744.64
Postage	739	341.33
Expired Insurance on Office Equipment	740	27.50
Depr. of Office Equipment	741	229.13
Social Security Taxes	742	349.25
State Unemployment Contributions	743	498.87
Misc. General Expense	744	117.95
		$39,581.93

PRACTICE ASSIGNMENT No. 37. ***Complete Report No. 37 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 38 is required.***

XXXVIII WORK SHEET

The trial balance of Bryant & Wood, taken as of May 31, will be used as the basis for illustrating the procedure in preparing a ten-column work sheet that will provide all of the information needed in preparing a balance sheet and a profit and loss statement. The completed work sheet of Bryant & Wood is reproduced on pages 518 and 519. The preparation of this work sheet involved the following procedure:

(a) The May 31 trial balance was copied on the work sheet, the debit and credit balances being recorded in the first two amount columns. It will be noted that this trial balance is the same as the one reproduced on page 513.

(b) The entries required in adjusting the account balances preliminary to preparing the financial statements as of May 31 were entered in the third and fourth amount columns. These columns were then footed and the footings were proved.

(c) The adjusted account balances were extended into the fifth and sixth amount columns. These columns were then footed and the footings were proved.

(d) The balances of the temporary accounts were extended into the seventh and eighth amount columns and these columns were footed. The difference between these footings, amounting to $8,056.71, was then recorded in the left-hand amount column as the net income for the eleven-months' period.

(e) The balances of the remaining accounts were extended into the ninth and tenth amount columns and the columns were footed. The difference between these footings, amounting to $8,056.71, was then recorded in the right-hand amount column as the net income for the eleven-months' period. The difference between the footings of the ninth and tenth amount columns is the same as the difference between the footings of the seventh and eighth amount columns.

(f) The totals of all the amount columns were then entered and the work sheet was ruled as shown in the illustration.

Adjustments. In preparing the work sheet for Bryant & Wood, it was necessary to analyze the accounts and to adjust any account balances that did not reflect the true value on May 31. The trial balance contains the general ledger accounts only. Since the operating expense accounts are kept in a subsidiary ledger and any necessary adjustments are made at the end of each month prior to taking a trial balance, no further adjustment of the operating expenses is required on the monthly work sheet.

Inventories. A comparison of the merchandise inventories, as reflected by the stock records on May 31, with the account balances shown in the May 31 trial balance reveals the following:

Merchandise Inventories	Dept. A	Dept. B
Per stock records	$31,254.06	$4,494.83
Per trial balance	21,847.90	3,121.13

The inventories shown in the May 31 trial balance represent the value of the goods in stock on July 1, the beginning of the current fiscal year.

A physical inventory was taken at the end of the preceding year and the value of the goods in stock was ascertained by multiplying the quantity of each item carried in stock by the cost price. Bryant & Wood use the "cost or market value, whichever is the lower" method of inventory valuation. The cost of each item was ascertained by reference to the most recent purchase invoices. Cost is used unless the current market value is found to be lower, in which case the market value is used. After multiplying the quantity of each item in stock by the unit cost price and after ascertaining the total cost it was necessary to add a portion of the transportation charges incurred. All transportation charges are charged to departmental transportation in accounts. At the end of each year the total transportation charges are divided by the total purchases to arrive at a rate which may be used in determining the amount of transportation charges to be added to the cost of the merchandise in stock. The rate ascertained at the end of the preceding year was found to be 1.75 per cent.

Since a physical inventory is taken at the end of each year only the monthly inventories are based on the stock records. Since the stock record shows the quantity of each item on hand it is only necessary to multiply the quantity by the unit cost price and to add the proper amount of transportation charges to ascertain the total value. Thus, the total value of the departmental inventories on May 31, based on the stock records, was ascertained as follows:

	Dept. A	Dept. B
Cost of merchandise on hand per stock records..	$30,716.52	$4,417.52
Add transportation charges @ 1.75%..........	537.54	77.31
Totals..................................	$31,254.06	$4,494.83

When financial statements are prepared monthly, it is customary to depend upon the stock records for the inventories. In most businesses it is impractical to take a physical inventory monthly; hence reliance is placed on the stock records for information as to the quantity of goods in stock at the end of each month. A physical inventory, however, should be taken at least at the end of each year. At that time, if the stock records are not in agreement with the physical inventories, it is customary to adjust the stock records in order to bring the book inventories into agreement with the physical inventories.

In addition to adjusting the inventory accounts, it is customary to ascertain the cost of merchandise sold in each department and to enter the cost of sales on the work sheet. The procedure in adjusting the inventory accounts and in recording the cost of sales for each department on the work sheet was as follows:

(a) The inventory for Dept. A, based on the stock records, was entered on the work sheet by debiting Merchandise Inventory, Dept. A and by crediting Cost of Sales, Dept. A for $31,254.06.

(b) The inventory for Dept. B, based on the stock records, was entered on the work sheet by debiting Merchandise Inventory, Dept. B and by crediting Cost of Sales, Dept. B for $4,494.83.

(c) The old or beginning inventory for Dept. A was transferred to Cost of Sales by debiting Cost of Sales, Dept. A and by crediting Merchandise Inventory, Dept. A for $21,847.90.

(d) The old or beginning inventory for Dept. B was transferred to Cost of Sales by debiting Cost of Sales, Dept. B and by crediting Merchandise Inventory, Dept. B for $3,121.13.

(e) The balances of the departmental purchases accounts were transferred to the cost of sales accounts by debiting Cost of Sales, Dept. A for $72,657.43 and Cost of Sales, Dept. B for $10,250.85 and by crediting Purchases, Dept. A for $72,657.43 and Purchases, Dept. B for $10,250.85.

(f) The balances of the departmental purchases returns and allowances accounts were transferred to the cost of sales accounts by debiting Purchases Returns and Allowances, Dept. A for $652 and Purchases Returns and Allowances, Dept. B for $36.35 and by crediting Cost of Sales, Dept. A for $652 and Cost of Sales, Dept. B for $36.35.

(g) The balances of the departmental accounts with transportation in were transferred to the cost of sales accounts by debiting Cost of Sales, Dept. A for $1,220.70 and Cost of Sales, Dept. B for $175.60 and by crediting Transportation In, Dept. A for $1,220.70 and Transportation In, Dept. B for $175.60.

BRYANT & WOOD

Work Sheet for Eleven-Months' Period Ended May 31, 19--

Accounts	Nos.	Trial Balance Dr.	Trial Balance Cr.	Adjustments Dr.	Adjustments Cr.	Adj. Trial Balance Dr.	Adj. Trial Balance Cr.	Profit and Loss Dr.	Profit and Loss Cr.	Balance Sheet Dr.	Balance Sheet Cr.
Liberty National Bank	111	7467 85				7467 85				7467 85	
Petty Cash Fund	112	50 00				50 00				50 00	
U. S. Treasury Bonds	12	9900 00				9900 00				9900 00	
Notes Receivable	131	3203 36				3203 36				3203 36	
Accounts Receivable	132	6671 87				6671 87				6671 87	
Reserve for Bad Debts	013		455 94				455 94				455 94
Mdse. Inv., Dept. A	14	21847 90		31254 06	21847 90	31254 06				31254 06	
Mdse. Inv., Dept. B	15	3121 13		4494 83	3121 13	4494 83				4494 83	
Accrued Interest Rec.	16	10 00		115 27		125 27				125 27	
Store Supplies	171	61 25				61 25				61 25	
Advertising Supplies	172	65 20				65 20				65 20	
Office Supplies	173	48 60				48 60				48 60	
Postage Stamps	174	8 80				8 80				8 80	
Prepaid Insurance	175	168 75				168 75				168 75	
Prepaid Fed. Excise Tax	176	2454 29				2454 29				2454 29	
Store Equipment	21	1543 50				1543 50				1543 50	
Res. for Depr. of S. E.	021		332 50				332 50				332 50
Delivery Equipment	22	1250 00				1250 00				1250 00	
Res. for Depr. of D. E.	022		476 04				476 04				476 04
Office Equipment	23	2660 00				2660 00				2660 00	
Res. for Depr. of O. E.	023		400 83				400 83				400 83
Fed. O-A Ins. Taxes Pay.	31		53 70				53 70				53 70
Fed. Unemp. Taxes Pay.	32		66 54				66 54				66 54
State U. C. Payable	33		90 70				90 70				90 70
Employees' Income Taxes Pay.	34		152 20				152 20				152 20
Notes Payable	35		3500 00				3500 00				3500 00
Accounts Payable	36		4790 10				4790 10				4790 10
Accrued Interest Pay.	37		22 50		11 92		34 42				34 42
Accrued Property Taxes Pay.	38		180 00				180 00				180 00
J. A. Bryant, Partner	41		27000 00				27000 00				27000 00

J. A. Bryant, Drawing	411	725 43				725 43				725 43	
W. L. Wood, Partner	42		27000 00				27000 00				27000 00
W. L. Wood, Drawing	421	436 62				436 62				436 62	
Sales, Dept. A	511		102634 44				102634 44		102634 44		
Sales Ret. & Allow., Dept. A	0511	1612 40				1612 40		1612 40			
Sales, Dept. B	512		19585 00				19585 00		19585 00		
Sales Ret. & Allow., Dept. B	0512	75 00				75 00		75 00			
Purchases Discount	521		1669 38				1669 38		1669 38		
Interest Income	522		129 38		115 27		244 65		244 65		
Purchases, Dept. A	61	72657 43			72657 43						
Purchases Ret. & Allow., Dept. A	061		652 00	652 00							
Purchases, Dept. B	62	10250 85			10250 85						
Purchases Ret. & Allow., Dept. B	062		36 35	36 35							
Transportation In, Dept. A	63	1220 70			1220 70						
Transportation In, Dept. B	64	175 60			175 60						
Operating Expenses	71	39581 93				39581 93		39581 93			
Sales Discount	751	1365 33				1365 33		1365 33			
Interest Expense	752	194 37		11 92		206 29		206 29			
Charitable Contributions	753	370 48				370 48		370 48			
Collection Expense	754	28 96				28 96		28 96			
Cost of Sales, Dept. A	65			21847 90	31254 06	63819 97		63819 97			
				72657 43	652 00						
				1220 70							
Cost of Sales, Dept. B	66			3121 13	4494 83	9016 40		9016 40			
				10250 85	36 35						
				175 60							
		189227 60	*189227 60*	*145838 04*	*145838 04*	*188666 44*	*188666 44*	*116076 76*	*124133 47*	*72589 68*	*64532 97*
		189227 60	189227 60	145838 04	145838 04	188666 44	188666 44	116076 76	124133 47	72589 68	64532 97
Net Income								8056 71			8056 71
								124133 47			*72589 68*
								124133 47	124133 47	72589 68	72589 68

It will be observed that after the foregoing adjustments were made, the balance of Cost of Sales, Dept. A, which was extended to the Adjusted Trial Balance Dr. column, amounted to $63,819.97 and the balance of Cost of Sales, Dept. B, which was extended to the Adjusted Trial Balance Dr. column, amounted to $9,016.40. These balances were arrived at by subtracting the sum of the credit entries from the sum of the debit entries.

Accruals. In order to determine whether the accounts with Accrued Interest Receivable and Accrued Interest Payable needed to be adjusted, it was necessary to ascertain the respective amounts of accrued interest receivable and accrued interest payable as of May 31. The notes receivable register was the source of the information needed in preparing the following schedule:

SCHEDULE OF ACCRUED INTEREST ON NOTES RECEIVABLE

No.	Principal Amount	Rate of Interest	Date of Note	Days Accrued	Accrued Interest
162	$750.00	6%	April 4	57	$ 7.13
163	450.00	...	April 2	..	......
165	500.00	6%	May 15	16	1.33
166	600.00	6%	May 20	11	1.10
167	401.60	6%	May 22	9	.60
168	201.76	...	May 16	..	......
169	300.00	6%	May 25	6	.30
Total interest accrued on notes receivable................					$10.46

In addition to the notes owned on May 31, Bryant & Wood owned 2½ per cent U. S. Treasury Bonds amounting to $9,900, acquired on December 1 of the preceding year, on which the interest is payable semi-annually June 15 and December 15. On May 31 interest on these bonds had been accruing for 167 days at 2½ per cent. Thus, the accrued interest on the bonds owned amounted to $114.81, to which was added the accrued interest on notes receivable amounting to $10.46, making the total accrued interest receivable on May 31, $125.27. Reference to the trial balance shows that the accrued interest receivable account had a debit balance of $10. This balance represented the amount of interest accrued at the close of the preceding fiscal year ended June 30. Since the interest accrued on May 31 amounted to $115.27 more than the account balance, it was necessary to adjust the account by debiting it for $115.27. The offsetting entry involved a credit to Interest Income for the same amount.

An analysis of the notes payable account revealed that there was outstanding a 90-day note for $3,500 dated April 2 and bearing interest at 6 per cent. On May 31 the interest on this note, which had been accruing for 59 days, amounted to $34.42.

Reference to the trial balance shows that the accrued interest payable account had a credit balance of $22.50. This balance represented the amount of interest accrued at the close of the preceding fiscal year ended June 30. Since the interest accrued on May 31 amounted to $11.92 more than the account balance, it was necessary to adjust the account by crediting it for $11.92. The offsetting entry involved a debit to Interest Expense for the same amount.

Adjusted Trial Balance Columns. After the required adjustments were entered on the work sheet, the adjusted account balances were extended to the Adjusted Trial Balance columns and the columns were footed to ascertain whether the debit and credit balances were equal in amount. This is an essential step in preparing a work sheet; it is important to ascertain that the debit and credit balances of the accounts are equal in amount before the accounts are classified by extending the balances to the columns headed Profit and Loss and Balance Sheet respectively.

Profit and Loss Columns. The balances of the temporary accounts only were extended to the columns headed Profit and Loss. Debit balances were entered in the left-hand amount column, while credit balances were entered in the right-hand amount column. After these account balances were extended, the Profit and Loss columns were footed, the difference between the footings was ascertained, and this difference, amounting to $8,056.71, was entered on the next horizontal line as the net income for the period. After the net income was entered, the footings of the Profit and Loss columns were found to be equal in amount.

To ascertain the amount of the net income for the month of May, it is only necessary to compare the net income shown on the work sheet for May with the net income shown on the work sheet for April. The net income shown on the work sheet for May represents the income for a period of eleven months, while the net income shown on the work sheet for April represents the income for a period of ten months. The net income for any month of the fiscal year may be ascertained in a similar manner.

Balance Sheet Columns. The last step in preparing the work sheet was to extend the balances of the remaining accounts from the Adjusted Trial

Balance columns to the Balance Sheet columns. Debit balances were entered in the left-hand amount column, while credit balances were entered in the right-hand amount column. After these account balances were extended, the Balance Sheet columns were footed, the difference between the footings was ascertained, and this difference, amounting to $8,056.71, was entered on the next horizontal line as the net income for the period. After the net income was entered, the footings of the Balance Sheet columns were found to be equal in amount.

A work sheet prepared in proper form accomplishes the following:

(a) Serves as a medium for making the necessary adjustments of the general ledger account balances preliminary to the preparation of financial statements.

(b) Facilitates the classification of the account balances on a basis of the statements to be prepared therefrom.

(c) Makes possible the ascertainment of the net income for the period.

PRACTICE ASSIGNMENT No. 38. Complete Report No. 38 in the workbook and submit your working papers to the instructor for approval. Then continue with the next study assignment in Unit Nineteen until Report No. 39 is required.

Unit Nineteen

PREPARING STATEMENTS AND CLOSING BOOKS

XXXIX THE FINANCIAL STATEMENTS

It is the function of accounting to record all of the transactions and the operations of a business that affect the assets, the liabilities, and the proprietorship. As an aid to management, the accounts should be analyzed periodically and statements should be prepared that will set forth the financial condition and the results of operations. In some cases an annual report only may be considered satisfactory. However, for the most efficient management of an enterprise, those concerned with its direction will not be content to wait until the end of the year to ascertain what has happened to the business during the year. Interim statements may be required semiannually, quarterly, or monthly as an aid to efficient management.

The accounts of Bryant & Wood are used as the basis for the discussion in this unit. The firm is organized as a partnership and the business is operated on the basis of a fiscal year ending June 30. It is the policy of the firm to require the preparation of a balance sheet and a profit and loss statement at the end of each month, supported by schedules of accounts receivable, accounts payable, operating expenses, and cost of sales.

The principal financial statements are the balance sheet and the profit and loss statement. These statements are complementary; that is, each correlates with the other and both should be taken into consideration in making an analysis of a business enterprise. The function and the form of the balance sheet and the profit and loss statement were discussed in detail in Unit Seven. The financial statements of Bryant & Wood are similar in form to the financial statements of W. L. Mann that were reproduced in that unit.

Balance Sheet. The balance sheet of Bryant & Wood prepared as of May 31 is reproduced on page 525. It was typed in account form. The information needed in preparing the balance sheet was obtained from the last two amount columns of the work sheet reproduced on pages 518 and 519. In preparing the work sheet the accounts were classified on a basis of (a) the profit and loss accounts and (b) the balance sheet accounts. In preparing the balance sheet, the accounts were further classified in accordance with standard practice. Reference to the balance sheet will show that the assets were classified into two groups: (a) current assets and (b) fixed assets. The liabilities were classified as current liabilities. Bryant & Wood had no fixed liabilities.

Interpreting the Balance Sheet. Interpretation of Bryant & Wood's balance sheet involves an analysis of the information summarized in it. The current assets consist of cash, marketable securities, receivables, inventories, accruals, and prepaid items. The order in which these items are listed is of considerable importance. Following cash, the assets are listed in the order in which they might most readily be converted into cash. This is sometimes referred to as their order of probable liquidity. In listing the notes receivable and the accounts receivable, the amount reserved for bad debts is shown as a deduction. The reserve is deducted from the total of notes receivable and accounts receivable because, when either a note or an account receivable becomes worthless, it is the practice of the firm to charge it to the reserve for bad debts.

The fixed assets of Bryant & Wood consist of three types of equipment: store equipment, delivery equipment, and office equipment. The book value of each type of equipment is shown separately. Since Bryant & Wood use the reserve method of accounting for depreciation, the credit balances of the reserve accounts are shown as deductions from the debit balances of the respective equipment accounts; thus, the net book value of each type of equipment is indicated.

When land and buildings are acquired for use in operating a business enterprise, they should be included among the fixed assets in the balance sheet. Separate accounts should be kept for different buildings and for different tracts or parcels of land. Reserves for depreciation of buildings should be shown in the balance sheet as deductions from the cost of the buildings so that the net book value of each building will be indicated.

Unused supplies, prepaid insurance, and prepaid federal excise taxes are listed among the current assets in the balance sheet. Sometimes these accounts are referred to as *deferred charges* and are listed last among the assets in the balance sheet. However, classifying these items as current assets is in accordance with the recommendation of the American Institute of Accountants.

(Continued on page 526)

BRYANT & WOOD

BALANCE SHEET, MAY 31, 19–

ASSETS

Current Assets:			
Cash		$ 7,517.85	
U. S. Treasury Bonds		9,900.00	
Notes Receivable	$ 3,203.36		
Accounts Receivable	6,671.87		
	$ 9,875.23		
Less Reserve for Bad Debts	455.94	9,419.29	
Merchandise Inventories:			
Dept. A	$31,254.06		
Dept. B	4,494.83	35,748.89	
Accrued Interest Receivable		125.27	
Supplies and Prepayments:			
Store Supplies	$ 61.25		
Advertising Supplies	65.20		
Office Supplies	48.60		
Postage Stamps	8.80		
Prepaid Insurance	168.75		
Prepaid Fed. Excise Tax	2,454.29	2,806.89	
Total Current Assets			$65,518.19
Fixed Assets:			
Store Equipment	$ 1,543.50		
Less Reserve for Depr.	332.50	$ 1,211.00	
Delivery Equipment	$ 1,250.00		
Less Reserve for Depr.	476.04	773.96	
Office Equipment	$ 2,660.00		
Less Reserve for Depr.	400.83	2,259.17	
Total Fixed Assets			4,244.13
Total Assets			$69,762.32

LIABILITIES

Current Liabilities:				
Social Security Taxes Payable:				
Federal Old-Age Ins. Taxes		$ 53.70		
Federal Unemployment Taxes		66.54		
State Unemploy. Contrib.		90.70	$ 210.94	
Employees' Income Taxes Pay			152.20	
Notes Payable			3,500.00	
Accounts Payable			4,790.10	
Accrued Interest Payable			34.42	
Accrued Property Taxes Pay			180.00	
Total Current Liabilities				$ 8,867.66

PROPRIETORSHIP

J. A. Bryant, Proprietorship, Beginning of Fiscal Period		$27,000.00		
Net Income (½ of $8,056.71)	$4,028.36			
Less Withdrawals during Period	725.43	3,302.93		
Proprietorship May 31, 19–			$30,302.93	
W. L. Wood, Proprietorship, Beginning of Fiscal Period		$27,000.00		
Net Income (½ of $8,056.71)	$4,028.35			
Less Withdrawals during Period	436.62	3,591.73		
Proprietorship May 31, 19–			30,591.73	
Total Proprietorship				60,894.66
Total Liabilities and Proprietorship				$69,762.32

Unused postage stamps and unexpired insurance can readily be converted into cash. Stamps may be redeemed at face value. If the unexpired insurance is canceled, the unused premium will be refunded; however, the amount of the refund will usually be somewhat less than the book value of the unexpired insurance because of the practice of insurance companies of charging a slightly higher rate on a short-term basis. Store supplies, advertising supplies, and office supplies may have little or no cash value; however, they are of value to a going business and they may be classified as current assets until they are consumed in the operation of the business.

The amount of the prepaid federal excise tax listed among the current assets in Bryant & Wood's balance sheet represents the amount of the tax applicable to the tires and tubes in stock on May 31. The tax is imposed on the manufacturer and is based on the weight of tires and tubes. It is the custom of tire manufacturers to bill the tax separately to the wholesaler, who in turn bills it separately to the retailer. Under this procedure, Bryant & Wood records the tax on tires and tubes purchased by debiting Prepaid Federal Excise Tax. When tires and tubes are sold by Bryant & Wood, the tax is credited to Prepaid Federal Excise Tax. Thus, the balance of the account always represents the tax applicable to the tires and tubes in stock. It is not practical to add the tax to the price of the tires and tubes because the tax is not subject to markup or discount.

All of the liabilities of Bryant & Wood are classified as current liabilities because they will mature within a comparatively short period of time. The prevailing practice is to classify as current liabilities all liabilities that are payable immediately or that will mature within the normal operating cycle of the business.

The liabilities of Bryant & Wood consist of social security taxes payable, employees' income taxes payable, notes payable, accounts payable, and accruals. The firm's liability for employees' income taxes payable arises from the fact that it is required to withhold a percentage of the wages of its employees and the amounts withheld are a liability until paid to the proper governmental agency.

Any debts that will not mature within the normal operating cycle of the business are usually listed in the balance sheet as fixed liabilities. Thus, long-term notes payable and mortgages payable that will not mature within a year should be listed in the balance sheet as fixed liabilities immediately following the current liabilities.

The proprietorship section of Bryant & Wood's balance sheet is arranged to show the proprietorship of each partner at the beginning and the end of the fiscal period. It was necessary to take into consideration (a) each partner's proprietorship at the beginning of the fiscal period and (b) his share of the net income for the period less the amount withdrawn during the period for personal use. Partners' withdrawals are not to be confused with partners' salaries. Under the terms of the partnership agreement, the salary of each partner must be treated as an operating expense in computing the net income. Any additional drawings for personal use should be considered as drawings in anticipation of profits. Had either partner withdrawn a sum greater than his share of the net income, it would have been necessary to show the excess drawings as a deduction from his proprietorship unless he reimbursed the partnership for the excess drawings. The salaries of the partners may be treated as an operating expense in computing the net income under the terms of the partnership agreement. However, it is important to understand that such salaries cannot be treated as a deductible expense in computing the net income of the partnership for federal income tax purposes.

Ratio Analysis. The total current assets of Bryant & Wood amount to $65,518.19, while the total current liabilities amount to $8,867.66. This is a ratio of 7.39 to 1. The ratio is found by dividing the total current assets by the total current liabilities. This ratio is important since in the ordinary course of a business the current liabilities must be paid out of the current assets. The fact that the firm has cash amounting to $7,517.85 while its total liabilities amount to only $8,867.66 indicates an excellent financial position. It is obvious that, during the current operating cycle, the firm will experience no difficulty in meeting its obligations as they mature unless something very unusual develops.

Working Capital. The amount invested in the current assets of a business represents the firm's gross working capital. The excess of the current assets over the current liabilities represents the firm's net working capital. The balance sheet of Bryant & Wood shows that they have a net working capital of $56,650.53 ($65,518.19 – $8,867.66). Of this amount $35,748.89 is invested in merchandise and $9,419.29 is represented by notes receivable and accounts receivable.

Invested Capital. As of May 31 the total capital invested by the partners amounted to $60,894.66. Since only $4,244.13 of the firm's capital was invested in fixed assets, it will be seen that most of the invested capital is available for use as working capital. This indicates a healthy financial condition.

Profit and Loss Statement. Bryant & Wood's profit and loss statement for the eleven-months' period ended May 31 is reproduced on page 529. The information needed in preparing this statement was obtained from the seventh and eighth amount columns of the work sheet reproduced on pages 518 and 519. The form of this statement is similar to the profit and loss statement of W. L. Mann that was reproduced on page 215. Since the firm is organized as a partnership, each partner's share of the net income is indicated at the bottom of the statement.

Interpreting the Profit and Loss Statement. The order in which the accounts are classified in the profit and loss statement aids in its interpretation. Merchants ordinarily derive the major part of their income from sales. Such income is commonly referred to as operating income. Bryant & Wood's gross profit on sales for the eleven-months' period ended May 31 amounted to $47,695.67. After operating expenses amounting to a total of $39,581.93 were deducted, the net operating income was found to be $8,113.74.

The income derived from other sources, amounting to a total of $1,914.03, was added to the net operating income, and other charges, amounting to $1,971.06, were subtracted from the sum to find the net income, which amounted to $8,056.71.

Percentage Analysis. It is common practice in analyzing a profit and loss statement on the percentage basis to let the net sales represent 100 per cent. On this basis Bryant & Wood's gross profit on sales amounted to approximately 39.57 per cent ($47,695.67 ÷ $120,532.04). Their net operating income amounted to 6.73 per cent, while their net income amounted to 6.68 per cent. In other words, every dollar of net sales resulted in a gross profit of 39.57 cents, a net operating income of 6.73 cents, and a net income of 6.68 cents.

The profit and loss statement of Bryant & Wood reveals an unusually large rate of gross profit on sales. This was due to an increase in the prices of the products handled by Bryant & Wood during the latter part of the period. Bryant & Wood uses the first-in, first-out method of valuing stock. Under this method the value of the goods in stock at the end of the period is based on the most recent purchases. As a result, the value of the inventory is higher than normal. For example, it will be noted that the inventory at the beginning of the year amounted to a total of only $24,969.03 while on May 31 it amounted to a total of $35,748.89. While the gross profit on sales for the period was abnormally high, there

(*Continued on page 530*)

BRYANT & WOOD

PROFIT AND LOSS STATEMENT FOR ELEVEN-MONTHS' PERIOD ENDED MAY 31, 19—

Operating Income:		
Department A—		
Sales	$102,634.44	
Less Returns and Allowances	1,612.40	
Net Sales	$101,022.04	
Less Cost of Sales	63,819.97	
Gross Profit on Sales		$37,202.07
Department B—		
Sales	$ 19,585.00	
Less Returns and Allowances	75.00	
Net Sales	$ 19,510.00	
Less Cost of Sales	9,016.40	
Gross Profit on Sales		10,493.60
Total Gross Profit on Sales		$47,695.67
Operating Expenses		39,581.93
Net Operating Income		$ 8,113.74
Other Income:		
Purchases Discount	$ 1,669.38	
Interest Income	244.65	
Total Other Income		1,914.03
		$10,027.77
Other Charges:		
Sales Discount	$ 1,365.33	
Interest Expense	206.29	
Charitable Contributions	370.48	
Collection Expense	28.96	
Total Other Charges		1,971.06
Net Income		$ 8,056.71
Distribution:		
J. A. Bryant	$ 4,028.36	
W. L. Wood	4,028.35	
	$ 8,056.71	

was an increase in the operating expenses for the period primarily because of increases in wages and taxes. As a result of the increased cost of doing business, the net income for the period amounted to only 6⅝ per cent of the net sales.

Rate of Turnover. For the eleven-months' period ended May 31, Bryant & Wood had a turnover 2.4. The rate of turnover was ascertained in the following manner:

Inventories at beginning of period	$24,969.03
Inventories at end of period	35,748.89
Total	$60,717.92
Average inventory ($60,717.92 ÷ 2)	30,358.96
Cost of sales for the period	72,836.37
$72,836.37 ÷ $30,358.96 = 2.4	

Ratio Analysis. Credit men and others concerned with the interpretation of financial statements often use ratio analysis as an aid to interpretation. Following is a brief explanation of the most commonly used ratios:

(a) *Ratio of current assets to current liabilities.* The purpose of this ratio is to determine the net working capital of a firm and its ability to meet its current obligations. This ratio is computed by dividing the total current assets by the total current liabilities.

As previously explained, Bryant & Wood's ratio of current assets to current liabilities on May 31 was approximately 7.39 to 1.

(b) *Ratio of merchandise to receivables.* An increase in the ratio of receivables to inventories tends to increase the total current assets. Inventories are usually computed at cost or market value, whichever is lower. On the other hand, receivables result from sales and hence represent selling values. This ratio is computed by dividing the total inventories by the total receivables.

Reference to Bryant & Wood's balance sheet as of May 31 will show that they had merchandise in stock amounting to $35,748.89 and receivables amounting to a total of $9,419.29. The ratio of merchandise to receivables, therefore, was approximately 3.8 to 1. The total receivables consisted of notes receivable amounting to $3,203.36 and accounts receivable amounting to $6,671.87 less a reserve for bad debts amounting to $455.94.

(c) *Ratio of net worth to fixed assets.* The excess of the net worth over the total value of the fixed assets indicates the amount of working capital provided by an individual in a sole proprietorship, by the partners in a partnership, or by the stockholders in a corporation. A comparison of this ratio over two or more successive years indicates whether too much of the profits may have been invested in fixed assets. This ratio is computed by dividing the net worth (proprietorship) by the total value of the fixed assets.

Reference to Bryant & Wood's balance sheet as of May 31 shows that the fixed assets amounted to a total of $4,244.13 and that the net worth of the partnership amounted to $60,894.66. The ratio of net worth to fixed assets, therefore, was approximately 14.35 to 1.

(d) *Ratio of net worth to indebtedness.* This ratio indicates the source of the total capital of the firm. Too large a proportion of indebtedness indicates insufficient invested capital. The proportion of invested capital is an important factor in measuring credit risk. This ratio is computed by dividing the net worth (proprietorship) by the total indebtedness.

Reference to Bryant & Wood's balance sheet as of May 31 shows that the net worth of the partnership amounted to a total of $60,894.66 and that the firm's total indebtedness amounted to $8,867.66. The ratio of net worth to indebtedness, therefore, was approximately 6.87 to 1.

(e) *Ratio of sales to receivables.* This ratio shows the average length of the collection period and indicates the speed with which collections are made. It helps to determine whether the ratio of current assets to current liabilities is sufficient or reasonable. This ratio is computed by dividing net sales by receivables.

Bryant & Wood's net sales for the eleven-months' period ended May 31 amounted to $120,532.04 and their receivables on May 31 amounted to $9,419.29. The ratio of sales to receivables, therefore, was slightly better than 12.8 to 1. This is an exceptionally favorable ratio.

(f) *Ratio of cost of sales to merchandise.* The purpose of this ratio is to determine the relative salability of merchandise. It is commonly referred to as the rate of turnover. The rate of turnover affects the margin of current assets over current liabilities. This ratio is computed by dividing cost of sales by the average inventory.

As previously explained, Bryant & Wood's rate of turnover for the eleven-months' period ended May 31 was 2.4.

(g) *Ratio of sales to net worth.* The purpose of this ratio is to determine whether the capital invested in the business is being used productively. This ratio may vary widely. Extremely high or low ratios may indicate an unsound condition. This ratio is computed by dividing the total net sales by the net worth.

Bryant & Wood's net sales for the eleven-months' period ended May 31 amounted to $120,532.04 and their net worth on May 31 amounted to $60,894.66. The ratio of sales to net worth, therefore, was approximately 2 to 1.

(h) *Radio of sales to fixed assets.* The purpose of this ratio is to determine whether the fixed assets are being fully utilized in the operation of the business. Excessive investments in plant and equipment may be revealed. This ratio is computed by dividing the total net sales by the sum of the fixed assets.

Bryant & Wood's net sales for the eleven-months' period ended May 31 amounted to $120,532.04 and their fixed assets on May 31 amounted to a total of $4,244.13. The ratio of sales to fixed assets, therefore, was approximately 28.4 to 1.

Schedules. The balance sheet and the profit and loss statement are usually supported by certain schedules, depending upon the amount of detailed information desired. It has been the policy of the accountant for Bryant & Wood to submit schedules of accounts receivable and accounts payable with the balance sheet and schedules of operating expenses and cost of sales with the profit and loss statement. The schedules of accounts receivable, accounts payable, and operating expenses prepared at the end of May are reproduced on pages 512 and 514. These schedules were prepared at the time of taking the trial balance as a means of proving the balances of the control accounts for accounts receivable, accounts payable, and operating expenses.

The work sheet provides the information needed in preparing schedules showing the cost of sales for each department. The schedules for the eleven-months' period ended May 31 follow.

BRYANT & WOOD

COST OF SALES, DEPT. A

Eleven-Months' Period Ended May 31, 19—

Merchandise Inventory, July 1 (beginning of period)		$21,847.90
Purchases	$72,657.43	
Less Purchases Returns and Allowances	652.00	
Net Purchases		72,005.43
Transportation In		1,220.70
Total Cost of Merchandise Available for Sale		$95,074.03
Less Merchandise Inventory, May 31 (end of period)		31,254.06
Cost of Sales		$63,819.97

BRYANT & WOOD

COST OF SALES, DEPT. B

Eleven-Months' Period Ended May 31, 19–

Merchandise Inventory, July 1 (beginning of period)		$ 3,121.13
Purchases	$10,250.85	
Less Purchases Returns and Allowances	36.35	
Net Purchases		10,214.50
Transportation In		175.60
Total Cost of Merchandise Available for Sale		$13,511.23
Less Merchandise Inventory, May 31 (end of period)		4,494.83
Cost of Sales		$ 9,016.40

PRACTICE ASSIGNMENT No. 39. Complete Report No. 39 in the workbook and submit your working papers to the instructor for approval. Then continue with the following study assignment until Report No. 40 is required.

XL CLOSING THE BOOKS

At the end of each year, it is customary to close the temporary accounts into a profit and loss summary account. Before the temporary accounts are closed, any necessary adjustments should be journalized and posted so that the account balances will reflect the true results of operations for the period.

The operating expense accounts of Bryant & Wood are kept in a subsidiary ledger with a control account in the general ledger. Any necessary adjustments in the operating expense accounts are made at the end of each month, the entries being journalized and posted in the usual manner. Under this plan, no further adjustment of the operating expense accounts is required at the end of the year.

Certain temporary accounts are kept in the general ledger. The only year-end adjustments required are those necessary to bring the general ledger accounts into agreement with the balance sheet and the profit and loss statement.

Adjusting the General Ledger Accounts. Since Bryant & Wood do not close their books until the end of the fiscal year, the adjusting entries appearing on the monthly work sheets are not posted to the general ledger accounts, except on June 30. Prior to June 30, the monthly work sheets are made solely as an aid in preparing the monthly statements required by the management. However, the June 30 work sheet also serves as an aid in preparing the annual report and in closing the books.

To illustrate the procedure in adjusting and closing the accounts at the end of the year, it will be assumed that Bryant & Wood's work sheet prepared as of May 31 and reproduced on pages 518 and 519 represents the year-end work sheet. On this assumption, the adjusting entries appearing on the work sheet should be journalized and posted to the proper general ledger accounts. The required entries are shown in the general journal reproduced on page 535. Since these entries affected the general ledger accounts only, individual posting is required. After the entries are posted, the general ledger account balances will be in complete agreement with the Adjusted Trial Balance columns of the work sheet reproduced on pages 518 and 519.

Closing the Temporary General Ledger Accounts. To close the temporary accounts, it is only necessary to transfer their balances to the profit and loss summary account. Assuming that the temporary accounts of Bryant & Wood are to be closed as of May 31, the work sheet reproduced on pages 518 and 519 provides the information needed in drafting the closing entries.

It will be noted that the income accounts are closed first, followed by the cost and expense accounts. It is also necessary to distribute the net income between the partners. The work sheet shows that the net income for the period amounted to $8,056.71. Under the partnership agreement, the partners share profits equally. Mr. Bryant has already withdrawn $725.43 and Mr. Wood $436.62. It is assumed that each partner wishes to have the remainder of his share of the net income transferred to his capital account.

The Profit and Loss Summary Account. In posting the closing entries, it is good accounting practice to write "P. & L." in the Items column of each temporary account as it is closed into the profit and loss summary account. It is also good practice to write the title of each temporary account in the Items column of the profit and loss summary account as it is posted. Reference to the profit and loss summary account reproduced on page 536 will show how this account appeared in Bryant & Wood's general ledger after the closing entries were posted and the account was ruled. The profit and loss summary account is a permanent ledger record that shows the results of operations for the accounting period. A comparison of the account with the profit and loss statement will reveal that they provide similar information differing only in form.

(Continued on page 536)

BRYANT & WOOD'S GENERAL JOURNAL FOR MONTH OF MAY, 19--

Debits: Operating Expenses Acct. No.	Debits: Operating Expenses Amount	✓	Debits: Accounts Payable	Debits: General Ledger Acct. No.	Debits: General Ledger Amount	✓	Day	Description	Credits: General Ledger Acct. No.	Credits: General Ledger Amount	✓	Credits: Accounts Payable	Credits: Accounts Receivable
							31	Adjusting Entries:					
				65	21847 90	√		To transfer beginning inventories to Cost of	14	21847 90	√		
				66	3121 13	√		Sales, Depts. A and B	15	3121 13	√		
				14	31254 06	√		To record ending inventories, Depts. A and B	65	31254 06	√		
				15	4494 83	√			66	4494 83	√		
				65	72657 43	√		To transfer purchases to Cost of Sales, Depts.	61	72657 43	√		
				66	10250 85	√		A and B	62	10250 85	√		
				65	1220 70	√		To transfer transportation in to Cost of Sales,	63	1220 70	√		
				66	175 60	√		Depts. A and B	64	175 60	√		
				061	652 00	√		To transfer purchases returns and allowances	65	652 00	√		
				062	36 35	√		to Cost of Sales, Depts. A and B	66	36 35	√		
				16	115 27	√		To adjust accrued interest receivable	522	115 27	√		
				752	11 92	√		To adjust accrued interest payable	37	11 92	√		
					145838 04					*145838 04*			
							31	Closing Entries:					
				511	102634 44	√		Sales, Dept. A — P. & L. Summary	43	102634 44	√		
				512	19585 00	√		Sales, Dept. B — " "	43	19585 00	√		
				521	1669 38	√		Purchases Discount — P. & L. Summary	43	1669 38	√		
				522	244 65	√		Interest Income — " "	43	244 65	√		
				43	1612 40	√		P. & L. Summary — Sales R. & A., Dept. A	0511	1612 40	√		
				43	75 00	√		" " — Sales R. & A., Dept. B	0512	75 00	√		
				43	63819 97	√		" " — Cost of Sales, Dept. A	65	63819 97	√		
				43	9016 40	√		" " — Cost of Sales, Dept. B	66	9016 40	√		
				43	39581 93	√		" " — Operating Expenses	71	39581 93	√		
				43	1365 33	√		" " — Sales Discount	751	1365 33	√		
				43	206 29	√		" " — Interest Expense	752	206 29	√		
				43	370 48	√		" " — Charitable Contribu.	753	370 48	√		
				43	28 96	√		" " — Collection Expense	754	28 96	√		
				43	725 43	√		" " — J. A. Bryant, Drawing	411	725 43	√		
				43	3302 93	√		" " — J. A. Bryant, Partner	41	3302 93	√		
				43	436 62	√		" " — W. L. Wood, Drawing	421	436 62	√		
				43	3591 73	√		" " — W. L. Wood, Partner	42	3591 73	√		
					394104 98					*394104 98*			

The profit and loss summary account is the accountant's ledger record of the operating results, while the profit and loss statement is the accountant's report of the operating results to the management.

PROFIT AND LOSS SUMMARY Account No. 43

19--				19--			
May 31	Sales R. & A., Dept. A	GJ535	1,612.40	May 31	Sales, Dept. A	GJ535	102,634.44
31	Sales R. & A., Dept. B	GJ535	75.00	31	Sales, Dept. B	GJ535	19,585.00
31	Cost of Sales, Dept. A	GJ535	63,819.97	31	Purchases Discount	GJ535	1,669.38
31	Cost of Sales, Dept. B	GJ535	9,016.40	31	Interest Income	GJ535	244.65
31	Operating Expenses	GJ535	39,581.93				*124 133.47*
31	Sales Discount	GJ535	1,365.33				
31	Interest Expense	GJ535	206.29				
31	Charitable Contrib.	GJ535	370.48				
31	Collection Expense	GJ535	28.96				
31	J. A. Bryant, Drawing	GJ535	725.43				
31	J. A. Bryant, Partner	GJ535	3,302.93				
31	W. L. Wood, Drawing	GJ535	436.62				
31	W. L. Wood, Partner	GJ535	3,591.73				
			124 133.47				
			124,133.47				124,133.47

Profit and Loss Summary Account Closed

Balancing and Ruling Accounts. After the adjusting and closing entries are posted, the temporary accounts will be in balance and should be ruled. It is also customary to balance and rule the partners' accounts and the bank checking account. Each partner's present worth or proprietorship should be brought down below the ruling; likewise, the balance in the bank checking account should be brought down below the ruling.

Closing the Operating Expense Ledger Accounts. After the closing entries are posted, all of the temporary accounts that are kept in the general ledger, including the operating expense control account, will be in balance. The operating expense accounts that are kept in the subsidiary ledger should also be closed. The procedure in closing an operating expense account is illustrated on pages 537 by reproducing the account with Advertising Expense. To close this account it was only necessary to write "P. & L." in the Items column, to enter the balance of the account in the Credits column, and to place a cipher in the Balance column. All of the accounts kept in the operating expense subsidiary ledger should be closed in like manner. When the balance form of account ruling is used, it is not necessary to rule an account that is in balance, although it may be ruled if desired.

ACCOUNT ADVERTISING EXPENSE ACCOUNT NO. 711

DATE	ITEMS	FOLIO	DEBITS	CREDITS	BALANCE
19--					
May 1	Dr. Balance	√			1,068.50
10		CD499	12.50		
31		CD500	3.50		
31		GJ507	28.35		1,112.85
31	P. & L.	√		1,112.85	-0-

Advertising Expense Account Closed

Post-Closing Trial Balance. After the closing entries are posted, a trial balance of the open accounts in the general ledger should be taken to test the equality of the debit and the credit balances. This trial balance is usually referred to as a post-closing trial balance. The post-closing trial balance for Bryant & Wood as of May 31 is reproduced below.

BRYANT & WOOD

POST-CLOSING TRIAL BALANCE, MAY 31, 19--

Accounts	Nos.	Dr.	Cr.
Liberty National Bank	111	$ 7,467.85	
Petty Cash Fund	112	50.00	
U. S. Treasury Bonds	12	9,900.00	
Notes Receivable	131	3,203.36	
Accounts Receivable	132	6,671.87	
Reserve for Bad Debts	013		$ 455.94
Merchandise Inventory, Dept. A	14	31,254.06	
Merchandise Inventory, Dept. B	15	4,494.83	
Accrued Interest Receivable	16	125.27	
Store Supplies	171	61.25	
Advertising Supplies	172	65.20	
Office Supplies	173	48.60	
Postage Stamps	174	8.80	
Prepaid Insurance	175	168.75	
Prepaid Federal Excise Tax	176	2,454.29	
Store Equipment	21	1,543.50	
Reserve for Depr. of Store Equipment	021		332.50
Delivery Equipment	22	1,250.00	
Reserve for Depr. of Delivery Equipment	022		476.04
Office Equipment	23	2,660.00	
Reserve for Depr. of Office Equipment	023		400.83
Federal Old-Age Insurance Taxes Payable	31		53.70
Federal Unemployment Taxes Payable	32		66.54
State Unemployment Contributions Payable	33		90.70
Employees' Income Taxes Payable	34		152.20
Notes Payable	35		3,500.00
Accounts Payable	36		4,790.10
Accrued Interest Payable	37		34.42
Accrued Property Taxes Payable	38		180.00
J. A. Bryant, Partner	41		30,302.93
W. L. Wood, Partner	42		30,591.73
		$71,427.63	$71,427.63

Reversing Entries. Some accountants follow the practice of reversing the adjusting entries for accruals. The reversing entries are usually made at the beginning of the succeeding accounting period before any transactions for the period are recorded in the accounts. The purpose of such reversing entries is to transfer the balances of the accounts with accruals to the proper operating accounts. This may facilitate the recording of subsequent routine transactions so that the proper amount of income will be credited to the period in which it is earned and the proper amount of expenses will be charged to the period in which they are incurred. Reference to Bryant & Wood's post-closing trial balance will show that the account with accrued interest receivable has a debit balance of $125.27 and that the account with accrued interest payable has a credit balance of $34.42. These balances resulted from the adjusting entries reproduced on page 535. If it is desired to reverse the adjusting entries for accrued interest receivable and accrued interest payable, the required entries may be made in general journal form as follows:

REVERSING ENTRIES

June 1.	Interest Income	$125.27	
	Accrued Interest Receivable		$125.27
	Accrued interest receivable transferred to Interest Income.		
1.	Accrued Interest Payable	34.42	
	Interest Expense		34.42
	Accrued interest payable transferred to Interest Expense.		

While the post-closing trial balance was dated on the last day of the accounting period (May 31), it should be noted that the reversing entries are dated on the first day of the succeeding period (June 1). When these reversing entries are posted, the accrued interest receivable account and the accrued interest payable account will be in balance; the interest income account will have a debit balance of $125.27, and the interest expense account will have a credit balance of $34.42.

The method of recording interest collected and interest paid during a period may be the same whether or not reversing entries are made to transfer accrued interest receivable to interest income and accrued interest payable to interest expense at the beginning of the period. The difference is in the method of recording the accruals at the end of the accounting period. When reversing entries are not made at the beginning of the period, it is necessary to record any increase or any decrease in the amounts of accrued interest receivable and accrued interest payable at the end of the period. When reversing entries are made at the beginning of the period, it is necessary to record the entire amounts of accrued interest receivable and of accrued interest payable at the end of the period.

For example, if Bryant & Wood found that accrued interest receivable at the end of the succeeding period amounted to $131.28 and reversing entries had not been made at the beginning of that period, it would be necessary to make an adjusting entry debiting Accrued Interest Receivable and crediting Interest Income for $6.01 (the amount of the increase in accrued interest receivable). If reversing entries had been made it would be necessary to make an adjusting entry debiting Accrued Interest Receivable and crediting Interest Income for $131.28 (the entire amount of accrued interest receivable).

As an aid in visualizing the effect of reversing entries, a comparison of the methods used by A and B in accounting for accrued interest receivable will be made. A narrative of the transactions completed by both parties appears on page 540. These transactions are recorded in the "T" accounts that follow the narrative.

A follows the practice of adjusting his accounts at the end of each year and of reversing the adjusting entries for accruals following the close of each year. B follows the practice of adjusting his accounts at the end of each year but does not reverse the adjusting entries for accruals.

A comparison of the accounts of A and B shows that the final results are the same under both methods. Since A reversed the adjusting entry for accrued interest receivable at the end of the first year, it was necessary for him to make an adjusting entry to record the entire amount of the interest accrued ($66.67) at the end of the second year. Since B did not reverse the adjusting entry for accrued interest receivable at the end of the first year, it was necessary for him to make an adjusting entry to record the increase in the amount of interest accrued ($33.34) at the end of the second year.

In the case of both A and B, adjusting entries may be required at the end of each year to record accrued interest receivable, but the amounts of the adjusting entries will vary because of the difference in their methods of accounting. The important thing to remember is that the balance of the account with accrued interest receivable must represent the true amount which may be classified as a current asset in the balance sheet at the end of the year. The balance of the account with interest income must represent the amount actually earned which may be included in the net income in the profit and loss statement for the year. In other words, under the accrual method of accounting interest income must be reported

NARRATIVE OF TRANSACTIONS

Sept. 2 (First Year)	Received two $1,000, 5% notes from a customer, one due in one year and the other due in eighteen months.
Dec. 31	Interest accrued on notes receivable, $33.33.
Sept. 2 (Second Year)	Received remittance for $1,050 in payment of a note for $1,000 and interest $50.
Dec. 31	Interest accrued on notes receivable, $66.67.

A'S ACCOUNTS

Notes Receivable

Sept.	2 (1st yr.)	1,000.00	Sept.	2 (2nd yr.)	1,000.00
	2 (1st yr.)	1,000.00			

Accrued Interest Receivable

Dec.	31 (1st yr.)	33.33	Jan.	1 (2nd yr.)	33.33
	31 (2nd yr.)	66.67			

Interest Income

Dec.	31 (1st yr.) P&L	33.33	Dec.	31 (1st yr.)	33.33
Jan.	1 (2nd yr.)	33.33	Sept.	2 (2nd yr.)	50.00
			Dec.	31 (2nd yr.)	66.67
				83.34	*116.67*

B'S ACCOUNTS

Notes Receivable

Sept.	2 (1st yr.)	1,000.00	Sept.	2 (2nd yr.)	1,000.00
	2 (1st yr.)	1,000.00			

Accrued Interest Receivable

Dec.	31 (1st yr.)	33.33			
	31 (2nd yr.)	33.34			
		66.67			

Interest Income

Dec.	31 (1st yr.) P&L	33.33	Dec.	31 (1st yr.)	33.33
			Sept.	2 (2nd yr.)	50.00
			Dec.	31 (2nd yr.)	33.34
					83.34

in the period in which it is earned. Any required adjustment of accrued interest receivable will also affect the interest income account.

The principles involved in the handling of adjusting and reversing entries for accrued interest receivable are also applicable to accrued interest payable. Any adjustment that is required to record an increase or a decrease of accrued interest payable at the end of the year will also affect the interest expense account.

In solving accounting problems involving accrued interest, it is always necessary to determine the balance of the accrued interest receivable and accrued interest payable accounts in order to determine whether the total amounts accrued represent increases or decreases in the account balances. It is only the amounts of any increases or any decreases that need be recorded. Of course, if the accounts with accrued interest receivable and accrued interest payable are in balance, the entire amount of any accrued interest receivable or accrued interest payable at the end of the year must be recorded by means of adjusting entries.

While this discussion has been confined to the handling of adjusting and reversing entries for accrued interest, the principles involved are also applicable to other accruals whether receivable or payable.

The Accounting Cycle. This unit completes another accounting cycle. Following is a brief outline of the various steps of this cycle:

(a) Journalizing all transactions chronologically.

(b) Posting to the general and subsidiary ledgers.

(c) Adjusting the operating expense accounts at the end of each month.

(d) Taking a trial balance of the general ledger accounts.

(e) Preparing a monthly work sheet and schedules of accounts receivable, accounts payable, and operating expenses.

(f) Preparing monthly financial statements, including a balance sheet and a profit and loss statement with schedules showing the departmental cost of sales.

(g) Adjusting the general ledger accounts and closing the books at the end of the year.

(h) Taking a post-closing trial balance at the end of the year.

PRACTICE ASSIGNMENT No. 40. Complete Report No. 40 in the workbook and submit your working papers to your instructor for approval. The instructor will then give directions as to the work to be done next.

PRACTICAL ACCOUNTING PROBLEMS

The problems in this unit are supplementary to those in the workbook. They are numbered to indicate the unit of the textbook with which they correlate. For example, Problems 11-A to 11-I, inclusive, correlate with Unit Eleven. Loose-leaf stationery should be used in solving these problems.

Problem 11-A

On May 1, E. H. Christman organized a photographic equipment and supplies enterprise and opened a new set of books. Following is a list of the assets that he invested in the business:

Cash	$ 7,212.95
Office Equipment	1,650.00
Store Equipment	2,195.40
Delivery Truck	2,480.00
Total	$13,538.35

He owed $640 on the delivery truck that was purchased on credit.
REQUIRED: Draft the opening entry in general journal form.

Problem 11-B

Henry Grim has been conducting a wholesale wallpaper and paint enterprise. He decides to install a new set of books as of January 2, based on his balance sheet of December 31 which follows:

HENRY GRIM
BALANCE SHEET, DECEMBER 31, 19--

ASSETS			LIABILITIES	
Cash		$ 2,212.75	Accounts Payable	$ 2,925.70
Accounts Rec.	$4,216.30		Social Security Taxes Payable	26.95
Less Res. for Bad Debts	312.48	3,903.82	Employees' Income Taxes Payable	62.12
Merchandise Inventory		8,196.54	Total Liabilities	$ 3,014.77
Prepaid Insurance		165.32	PROPRIETORSHIP	
Store Equipment	$3,200.00			
Less Res. for Depr.	290.00	2,910.00	Henry Grim, Proprietor	14,373.66
Total Assets		$17,388.43	Total Liabilities and Prop.	$17,388.43

REQUIRED: Draft the opening entry in general journal form.

Problem 11-C

E. R. Duncan is engaged in the wholesale leather goods business. After closing his temporary proprietorship accounts for the calendar year ended December 31, his profit and loss summary account had a credit balance of $9,250.45. At the same time his capital account had a credit balance of $29,745 and his drawing account had a debit balance of $6,000.

REQUIRED: (a) Using the standard account form of ledger paper, open Mr. Duncan's capital account and drawing account, and a profit and loss summary account, and enter the December 31 balances. (b) Assuming that Mr. Duncan wishes both the profit and loss summary and drawing accounts closed, and the profits, not previously withdrawn, transferred to his capital account as an addition to his investment, make the required entries in the accounts. Total and rule the accounts and bring down Mr. Duncan's present capital below the ruling.

Problem 11-D

Mark H. Walker has been operating a wholesale hardware business as a sole proprietor. His balance sheet prepared as of September 30 is reproduced below. On October 1 of the current year he admits Charles M. Coulter as a partner with a one half interest in the business to be conducted under the firm name of Walker & Coulter. Under the partnership agreement, Mr. Coulter invests $10,866.92 in cash. The assets of Mr. Walker become the property of the partnership and his liabilities are assumed by the partnership.

MARK H. WALKER

BALANCE SHEET, SEPTEMBER 30, 19--

ASSETS			LIABILITIES	
Cash		$ 3,260.12	Notes Payable	$ 2,500.00
Accounts Rec.	$3,800.40		Accounts Payable	2,100.50
Less Res. for Bad Debts	390.00	3,410.40	Social Security Taxes Payable	24.00
			Employees' Income Taxes Payable	56.00
Merchandise Inventory		7,296.90		
Store Equipment	$2,100.00		Total Liabilities	$ 4,680.50
Less Res. for Depr.	520.00	1,580.00	PROPRIETORSHIP	
			Mark H. Walker, Proprietor	10,866.92
Total Assets		$15,547.42	Total Liabilities and Prop.	$15,547.42

REQUIRED: Assuming that a new set of books is installed by the partnership, draft the necessary opening entries in general journal form to record the investments of the partners.

Problem 11-E

William A. Bence and J. A. Womack have been competitors in the wholesale drug business. On July 1 of the current year they form a partnership, to be operated under the firm name of Bence & Womack. Their balance sheets as of June 30 are reproduced below. The partnership agreement provides that the assets are to be taken over at their book value and that the liabilities are to be assumed by the partnership. The agreement also provides that Mr. Womack is to contribute a sufficient amount of additional cash to make his investment equal to Mr. Bence's investment. It is also agreed that the partners will share profits and losses equally and the assets will be distributed equally between them in case of dissolution.

WILLIAM A. BENCE

BALANCE SHEET, JUNE 30, 19--

Assets			Liabilities	
Cash		$ 3,100.95	Notes Payable	$ 900.00
Accounts Rec.	$2,850.20		Accounts Payable	2,140.12
Less Res. for Bad Debts	57.40	2,792.80	Social Security Taxes Payable	24.00
Merchandise Inventory		4,690.87	Employees' Income Taxes Payable	59.00
Delivery Equip.	$3,100.00		Total Liabilities	$ 3,123.12
Less Res. for Depr.	775.00	2,325.00		
Office Equipment	$1,200.00		Proprietorship	
Less Res. for Depr.	400.00	800.00	William A. Bence, Proprietor	10,586.50
Total Assets		$13,709.62	Total Liabilities and Prop.	$13,709.62

J. A. WOMACK

BALANCE SHEET, JUNE 30, 19--

Assets			Liabilities	
Cash		$ 4,200.30	Accounts Payable	$ 2,109.65
Accounts Rec.	$2,100.99		Social Security Taxes Payable	22.00
Less Res. for Bad Debts	49.60	2,051.39	Employees' Income Taxes Payable	52.46
Merchandise Inventory		3,240.65	Total Liabilities	$ 2,184.11
Delivery Equip.	$2,800.00			
Less Res. for Depr.	700.00	2,100.00	Proprietorship	
Office Equipment	$1,000.00		J. A. Womack, Proprietor	10,108.23
Less Res. for Depr.	300.00	700.00		
Total Assets		$12,292.34	Total Liabilities and Prop.	$12,292.34

REQUIRED: Assuming that a new set of books is installed by the partnership, draft the necessary opening entries in general journal form to record the investments of the partners.

Problem 11-F

The Westervelt Upholstering Co., a partnership, is engaged in the wholesale upholstering business. Ownership of the company is vested in J. C. Westervelt, R. C. Crays, A. T. Collard, and A. C. Thompson. Profits and losses are shared equally.

Mr. Collard died on July 5. His widow is entitled to receive his share in the distribution of the partnership assets. The remaining partners agreed to buy his widow's interest at 93% of its book value. When the books were closed as of the date of Mr. Collard's death his capital account had a credit balance of $8,516.20. On August 15 a partnership check was issued to Mrs. Collard in final settlement.

REQUIRED: Compute the amount to be paid Mrs. Collard under the agreement and draft the general journal entry required to record the check in the books of the partnership.

Problem 11-G

January 1. The Ideal Carpet Co. was incorporated with an authorized issue of 1,000 shares of common capital stock, par value $25 per share. Subscriptions, accompanied by checks, were received from the following:

A. D. Geissler, 300 shares, $7,500
L. F. Geissler, 300 shares, $7,500
P. G. Cameron, 200 shares, $5,000
L. L. Gleason, 200 shares, $5,000

Following is a list of the corporate accounts to be kept:

Unissued Capital Stock	Subscriptions Receivable
Authorized Capital Stock	Capital Stock Subscribed

REQUIRED: Draft the general journal entries required to record (a) the authorized issue of common stock, (b) the stock subscriptions received, (c) cash received to apply on subscriptions, and (d) the capital stock issued to subscribers on January 10.

Problem 11-H

August 28. The board of directors of The Atlantic Rolling Mill Co. declared a dividend of $1.25 per share, payable out of surplus, on its 4½% cumulative preferred stock, payable October 16 to holders of record September 15. There were 21,320 shares of this stock outstanding.

October 16. The company mailed dividend checks to stockholders amounting to a total of $26,650.

REQUIRED: Using standard two-column journal paper, record (a) the dividend declared on August 28 and (b) the dividend paid on October 16.

Problem 11-I

William Fuqua, Charles Lee, and Everett Hulse were engaged in business as a partnership under the firm name of Fuqua, Lee & Hulse. On January 2, The Midwest Distributing Co., with an authorized capital of $50,000 consisting of 5,000 shares of common capital stock, par value $10 per share, was organized to take over the business formerly conducted by the partnership. The following balance sheet of the partnership was prepared at the time of incorporating the business:

FUQUA, LEE & HULSE
BALANCE SHEET, DECEMBER 31, 19--

Assets			Liabilities	
Cash		$ 6,590.42	Accounts Payable	$ 3,509.60
Accounts Rec.	$7,650.98		Social Security Taxes Payable	33.40
Less Res. for Bad Debts	712.00	6,938.98	Employees' Income Taxes Payable	61.12
Merchandise Inventory		11,612.30	Total Liabilities	$ 3,604.12
Office Equipment	$2,200.00			
Less Res. for Depr.	700.00	1,500.00	Proprietorship	
			William Fuqua, Partner	9,202.12
Delivery Equip.	$2,100.00		Charles Lee, Partner	8,005.60
Less Res. for Depr.	700.00	1,400.00	Everett Hulse, Partner	7,229.86
Total Assets		$28,041.70	Total Liabilities and Prop.	$28,041.70

The partners subscribed for capital stock of the corporation as follows:

William Fuqua, 2,000 shares at $10 a share	$20,000
Charles Lee, 2,000 shares at $10 a share	20,000
Everett Hulse, 1,000 shares at $10 a share	10,000

The partners, as individuals, received credit toward their subscriptions for their respective equities in the assets of the partnership and issued their personal checks for the balance of their respective subscriptions. A new set of books is to be installed by the corporation.

REQUIRED: Draft entries in general journal form to record the following: (a) The organization of the corporation, (b) the transfer of the accounts of the partnership to the corporation, (c) the receipt of cash from the partners in payment of the balances due on their respective subscriptions, and (d) the issuance of stock certificates to the partners.

Problem 12-A

Nichols & Sellers are partners engaged in the wholesale distribution of office furniture and supplies. The merchandise accounts are kept on the departmental basis, Dept. A comprising furniture and Dept. B all other merchandise. The following general ledger accounts are affected by this problem:

21 Store Equipment	61 Purchases, Dept. A
22 Office Equipment	62 Purchases, Dept. B
35 Notes Payable	63 Transportation In, Dept. A
36 Accounts Payable	64 Transportation In, Dept. B

Following is a narrative of purchases made during February:

Feb. 1. (Tuesday) No. 206, The Shaw-Walker Co., Washington; desks, \$316.40; terms, January 27 — 2/10, n/30; Pennsylvania freight collect.

No. 207, Utility Supply Co., City; memo books, \$47.75; terms, January 28 — 2/10, n/30.

No. 208, Office Supply Co., Chicago; ledger outfits, \$119.50; terms, January 28 — 2/10, n/60; postage prepaid and added to invoice, \$6.20.

No. 209, Indian Splint, Inc., Rochester; chairs, \$49.30; terms, January 28 — 3/10, n/30; New York Central freight collect.

No. 210, Hekman Furniture Co., Grand Rapids; tables, \$89.55; terms, January 27 — 30 days; Pere Marquette freight collect.

14. No. 211, The Wickwede Bros. Co., Marietta; tables, \$55; terms, February 11 — 30 days; Big Four freight prepaid and added to invoice, \$5.20.

No. 212, Waterman's, New York City; desk sets, \$198.20; terms, February 10 — 30 days; express prepaid and added to invoice, \$13.95.

21. No. 213, The Shaw-Walker Co., Washington; filing cabinets (for store use), \$204; terms, February 18 — 2/10, n/30; Pere Marquette freight collect.

Received a corrected purchase invoice, dated January 27, from Hekman Furniture Co., Grand Rapids, \$90.55. (See purchase invoice No. 210.)

No. 214, High Point Furniture Co., High Point; desks, \$275; terms, February 19 — 30-day note with interest at 6%.

28. No. 215, Royal Typewriter Co., City; typewriter (for office use) \$105; terms, February 26 — 30 days.

Required: As the accountant for the partnership (a) enter each invoice in an invoice record similar to the one reproduced on page 341 (except that a column will not be required for federal excise tax), and post direct to the proper creditor's account in a subsidiary accounts payable ledger; (b) complete the individual posting from the invoice record to the general ledger; (c) foot, prove the footings, enter the totals, and rule the invoice record; (d) complete the summary posting; and (e) prove the balance of the accounts payable account by preparing a schedule of the accounts with creditors as of February 28. Use standard ledger paper for the general ledger and balance-column ledger paper for the accounts payable ledger.

Problem 13-A

Beetle and Sparks are partners engaged in the wholesale distribution of musical instruments. The merchandise accounts are kept on the departmental basis. Following is a list of the general ledger accounts that are affected by this problem, with the September 1 balances indicated:

131 Notes Receivable, \$700
132 Accounts Receivable, \$1,125.40
511 Sales, Dept. A, \$7,693.12
0511 Sales Returns and Allowances, Dept. A, \$375.40
512 Sales, Dept. B, \$6,212.92
0512 Sales Returns and Allowances, Dept. B, \$113.45
719 Transportation Out, \$219.40

As of September 1, Beetle and Sparks' accounts receivable had debit balances as follows:

Gaddis & Wallace, 12 Main Street, Evansville; \$220
Hamilton Bros., 46 Spruce Street, Quincy; \$198.40
Herron's Department Store, 1240 Main Street, Lafayette; \$215.90
Moberly & Son, 262 Division Street, Janesville; \$212.32
Tull's Department Store, 315 Virginia Avenue, Decatur; \$278.78

All charge sales are subject to a discount of 2% if paid within ten days from date of invoice, net 30 days.

Following is a narrative of the charge sales for September:

Sept. 1. (Friday) Sale No. 162, Tull's Department Store; Dept. A, \$82.60.
2. Sale No. 163, Moberly & Son; Dept. B, \$96.40. Express prepaid and added to invoice, \$4.50.
5. Sale No. 164, Gaddis & Wallace; Dept. A, \$42.50; Dept. B, \$32.40.
8. Sale No. 165, E. D. Carpenter, 2715 Bigbee, Bowling Green; Dept. A, \$104.60.
11. Sale No. 166, Hamilton Bros.; Dept. A, \$76.20; Dept. B, \$14.30. Freight prepaid and added to invoice, \$4.65.
13. Sale No. 167, Tull's Department Store; Dept. A, \$85; Dept. B, \$165.30.
15. Sale No. 168, Lilly & Dunscomb Furniture Store, 12 Green Street, Fond du Lac; Dept. B, \$54.20. Express prepaid and added to invoice, \$2.12.
16. Sale No. 169, Herron's Department Store; Dept. A, \$49.50; Dept. B, \$42.60.

Sept. 18. Sent E. D. Carpenter a corrected invoice for Sale No. 165 amounting to $106.40.

20. Sale No. 170, Carr's Victrola Shop, 22 Bloomfield Street, Paducah; Dept. A, $112.50; received 60-day, 5% interest-bearing note.

22. Sent Lilly & Dunscomb Furniture Store a corrected invoice for Sale No. 168 amounting to $57.32.

27. Sale No. 171, Tull's Department Store; Dept. A, $22.90. Parcel post charges added to invoice, $1.67.

28. Sale No. 172, Moberly & Son; Dept. A, $27; Dept. B, $32.40. Less credit for merchandise returned, Dept. A, $6.90.

30. Sale No. 173, Gaddis & Wallace; Dept. B, $92. Freight prepaid and added to invoice, $3.43.

REQUIRED: (a) Using standard ledger paper, open the necessary general ledger accounts and enter the September 1 balances. (b) Using balance-column ledger paper, open the necessary accounts receivable ledger accounts and enter the September 1 balances. (c) Using a sales record similar to the one reproduced on page 365 (except that a column will not be required for federal excise tax), enter the charge sales for September and post direct to the proper customers' accounts. (d) Complete the individual posting from the sales record to the general ledger accounts. (e) Foot, prove the footings, enter the totals, and rule the sales record; complete the summary posting. (f) Foot the general ledger accounts and prove the balance of the accounts receivable account by preparing a schedule of the accounts with customers as of September 30.

Problem 13-B

Wilson's Washing Machine Shop uses the installment method of accounting for sales of washing machines on an installment payment basis. The following information was obtained from the general ledger accounts at the end of the current year:

Installment Sales	$16,250.00
Cost of Sales	13,000.00
Total down payments and collections from installment customers	12,250.00

REQUIRED: (a) Ascertain the amount of gross profit to be realized on the installment sales. (b) Ascertain the percentage of the gross profit to be realized on the installment sales. (c) Ascertain the amount of gross profit actually realized during the year. (d) Draft an entry in general journal form to close the installment sales account at the end of the year.

Problem 13-C

The Graybar Electric Co. distributes electric motors to local dealers on the consignment basis. Shipments to dealers on consignment are charged to the consignees at list prices. The dealer's basic compensation is a trade discount of 25% from the list prices. The dealer is also allowed an additional discount of 5% for payment in full on or before the 5th of the month for merchandise sold during the preceding month.

On October 2, The Graybar Electric Co. made a shipment of electric motors to Garvin & Son on consignment. The invoice of shipment amounted to a total of $665, computed at retail prices. During October, Garvin & Son sold all of the electric motors that were consigned to them on the October 2 shipment. On November 5, Garvin & Son rendered a statement of consignment sales to The Graybar Electric Co., at the same time remitting the proceeds which were computed as follows:

Sales		$665.00
Less:		
Commission, 25%	$166.25	
Cash discount, 5%	24.94	191.19
Proceeds		$473.81

REQUIRED: (a) As the accountant for The Graybar Electric Co. draft the entries in journal form necessary to record (1) the invoice of shipment to Garvin & Son on October 2 and (2) the sale of consigned merchandise by Garvin & Son during October, per statement received November 5 with remittance for $473.81 in payment of the proceeds. (b) Assuming that you are one of the partners of Garvin & Son and keep the books, draft the entries in general journal form required to record (1) the invoice of shipment received from The Graybar Electric Co. on October 2 and (2) the sale of consigned merchandise during October, per statement rendered November 5 with a check for $473.81 in payment of the proceeds.

Problem 14-A

Moberly & Hamilton are wholesale dealers in china and glassware. In accounting for notes, they use a notes receivable register similar to the one reproduced on pages 398 and 399. Following is a narrative of transactions involving notes received from customers during the current year:

Mar. 6. Received from Charles Lahke a 60-day, 6% note (No. 1) for $400 dated March 4 and payable at First National Bank, Cedar Rapids.

April 26. Received from Robert W. Nelson a 90-day, 5% note (No. 2) for $300 dated April 25 and payable at Second National Bank, Meadville.

May 3. Received a check for $404 from Charles Lahke in payment of his note due today plus interest.

19. Received from Louis A. Finch a 60-day, 6% note (No. 3) for $250 dated May 18 and payable at Hyde Park Trust Company, Hyde Park.

July 17. Received a check for $252.50 from Louis A. Finch in payment of his note due today plus interest.

24. Received a check for $303.75 from Robert W. Nelson in payment of his note due today plus interest.

Oct. 2. Received from R. K. Chapman a 90-day, 5% note (No. 4) for $460 dated October 2 and payable at Windsor State Bank.

19. Discounted R. K. Chapman's note for $460 at the Shelby Loan & Trust Company at 6% and received credit for the proceeds.

REQUIRED: (a) Draft the entries in general journal form to record the foregoing transactions. Foot the amount columns as a means of proof. (b) Make the required entries in a notes receivable register to provide a detailed auxiliary record of the notes received by Moberly & Hamilton.

Problem 14-B

Baker & Herron operate a department store. Sometimes they find it necessary to issue notes to creditors to obtain extensions of time on accounts payable. Unless otherwise stated all such notes are made payable at the Shelby County State Bank, Shelbyville. Following is a narrative of transactions involving notes issued by Baker & Herron during the current year:

Feb. 1. Borrowed $500 from the bank on a 90-day, 5% note (No. 1).

Mar. 7. Issued a 60-day, 6% note (No. 2) for $295 to Alms & Doepke Co.

April 20. Issued a 60-day, 5% note (No. 3) for $320 to S. P. Nelson & Sons.

May 2. Issued a check for $506.25 to the bank in payment of note due today plus interest.

6. Gave Alms & Doepke Co. a check for $2.95 in payment of the interest and a new note (No. 4) for $295, due in 60 days, with interest at 6%, in settlement of the note due today.

June 19. Issued a check for $322.67 to S. P. Nelson & Sons in payment of note due today plus interest.

July 1. Borrowed $1,000 from the bank on a 90-day, 5% note (No. 5).

5. Issued a check for $297.95 to Alms & Doepke Co. in payment of note due today plus interest.

Sept. 29. Gave Shelby County State Bank a check for \$12.50 in payment of the interest and a new note (No. 6) for \$1,000, due in 60 days, with interest at 5%, in settlement of the note due today.

Nov. 28. Issued a check for \$1,008.33 to the bank in payment of note due today plus interest.

REQUIRED: (a) Draft the entries in general journal form to record the foregoing transactions. Foot the amount columns as a means of proof. (b) Make the required entries in a notes payable register similar to the one reproduced on pages 404 and 405, to provide a detailed auxiliary record of the notes issued by Baker & Herron.

Problem 14-C

Crockett & Hyde are engaged in the wholesale distribution of dairy products. Following is a narrative of selected transactions completed by the firm:

April 18. Received a cashier's check from The National Bank of Wilmette for \$216 in payment of a sight draft for \$216.50 drawn April 14 on Daniel Laurence, a customer, less 50 cents collection charges.

June 9. Received an accepted time draft, dated June 7 for 30 days, for \$112.92 from L. B. Ratterman in temporary settlement of his account.

July 9. Received a cashier's check from The Second National Bank for \$112.42 in payment of the time draft for \$112.92 drawn on L. B. Ratterman, June 7 and accepted on June 9, less 50 cents collection charges.

Aug. 23. Received trade acceptance, No. 22, dated August 17, payable September 15, from J. S. Turner for \$495.16.

26. Discounted the foregoing trade acceptance at The Atlas National Bank, at a discount of 4% and deposited the proceeds.

REQUIRED: (a) Record the foregoing transactions in general journal form. Foot the amount columns as a means of proof. (b) Open an account with Notes Receivable, Account No. 131; post the journal entries affecting this account; foot the amount columns, and if the account is found to be in balance, rule the account.

Problem 14-D

Urban & Wiley are wholesale distributors of plate and window glass. Following is a narrative of selected transactions completed by the firm:

Mar. 28. Accepted a sight draft for \$250 drawn by Pittsburgh Plate Glass Co., a creditor, and issued a check in payment.

April 19. Accepted a time draft for $316.45, dated April 17 at 30 days' sight, drawn by Kellogg & Kidd, creditors.

May 19. Issued a check for $316.45 in payment of time draft accepted April 19.

Sept. 5. Honored a trade acceptance drawn by Libbey, Owens, Ford Glass Co., a creditor, on September 2 for $210, payable on October 2.

Oct. 2. Issued a check for $210 in payment of the foregoing trade acceptance.

REQUIRED: (a) Record the foregoing transactions in general journal form. Foot the amount columns as a means of proof. (b) Open an account with Notes Payable, Account No. 35; post the journal entries affecting this account; foot the amount columns, and if the account is found to be in balance, rule the account.

Problem 15-A

Bush & Hayt operate a mail-order house as partners. Metered postage is used on parcel post packages. As required, deposits are made for postage under the permit system. Postage stamps are purchased for other purposes. All prepaid postage is charged to Postage Stamps, Account No. 174, and periodically the postage used is charged to the following expense accounts:

719 Transportation Out (Parcel Post)
724 Postage on Advertising Matter
739 Postage on General Mail

Before adjusting entries had been made on April 30, the postage stamps account had a debit balance of $960.

REQUIRED: (a) Open the necessary accounts and enter the balance of the postage stamps account before adjustment. (b) Assuming that (1) during the month of April the postage used on parcel post packages amounted to $298 and on advertising matter, $275; and (2) that on April 30 the unused stamps on hand amounted to $85 and the unused metered postage amounted to $145, make the required adjusting entry in general journal form to record all postage expense for the month. (c) Post. (d) Balance and rule the postage stamps account and bring down the balance as of May 1.

Problem 15-B

Beginning on January 3 of the current year Kimball & Cleveland engaged as partners in the distribution of nonalcoholic beverages. In accounting for insurance, the following accounts are used:

175 Prepaid Insurance
720 Expired Insurance on Merchandise
721 Expired Insurance on Store Equipment
740 Expired Insurance on Office Equipment

The premiums paid for insurance are charged to the prepaid insurance account. At the end of each month the expired insurance is charged to the proper expense accounts and credited to Prepaid Insurance. The firm keeps an auxiliary record of insurance in the form of a register similar to the one on pages 424 and 425.

Following is a record of the insurance transactions completed during the current year:

Jan. 3. Paid the premiums on the following insurance policies:
No. 72420 dated January 1, General Accident, Fire & Life Insurance Co.; merchandise, $30,000; terms, one year; premium, $201.60.
No. 62412A dated January 1, Hardware Mutual Insurance Company of Minnesota; merchandise, $5,000; term, three years; premium, $90.
No. 247380 dated January 1, Lumbermen's Mutual Insurance Co.; office equipment, $1,500; term, one year; premium, $9.
No. 42416 dated January 1, Mutual Fire Insurance Co.; store equipment, $1,000; term, one year; premium, $7.20.

Feb. 2. Paid $60 premium on insurance policy No. 112490 dated February 1, Hartford Fire Insurance Co.; merchandise, $8,000; term, one year.

Mar. 6. Paid $18 premium on insurance policy No. 46230 dated March 1, Merrimac Mutual Fire Insurance Co.; merchandise, $1,000; term, three years.

Sept. 12. Received a check for $18 from the Hartford Fire Insurance Co. representing a refund on policy No. 112490 canceled as of September 1.

Nov. 10. Paid $15 premium on insurance policy No. 16230 dated November 1, Sun Mutual Fire Insurance Co.; store equipment, $2,000; term, one year.

REQUIRED: (a) Journalize the transactions involving the premiums paid on policies purchased during January; enter the policies on the left-hand page of an insurance register form; extend the proper proportion of the premium on each policy in effect during January to the January column on the right-hand page of the register; foot the column in small pencil figures. (b) Draft a journal entry to record the amount of the insurance expired during January. (c) Continue the work required each month to record any new insurance purchased during the month and to record the total insurance expired during the month. In recording the transactions for September, it will also be necessary to draft a journal entry to record the amount refunded on September 12 on policy No. 112490. (d) As of December 31, enter the expired and unexpired insurance on each policy in the last two columns on the right-hand page of the insurance register and foot the columns in small pencil figures. (e) Open an account for Prepaid Insurance, Account No. 175. Post from the general journal the debit and credit entries affecting the prepaid insurance account. After completing the posting to the prepaid insurance account, foot the amount columns, ascertain the balance, and enter it on the proper side of the account in small pencil figures. Prove your work by comparing the balance of the account with the footing of the unexpired insurance column on the right-hand page of the insurance register.

Problem 15-C

On February 1 of the current year Trees & Walmsley engage in the wholesale distribution of air-conditioning equipment as partners. In accounting for their fixed assets, the following accounts are used:

21 Store Equipment
  021 Reserve for Depreciation of Store Equipment
22 Delivery Equipment
  022 Reserve for Depreciation of Delivery Equipment
23 Office Equipment
  023 Reserve for Depreciation of Office Equipment
36 Accounts Payable
725 Depreciation of Store Equipment
726 Depreciation of Delivery Equipment
741 Depreciation of Office Equipment

Transactions involving the purchase of fixed assets on credit are recorded in an invoice record from which they are posted to the proper general ledger accounts. Accounts with creditors are kept in a subsidiary accounts payable ledger and the posting to these accounts is done directly from the invoices and other vouchers representing transactions completed with creditors. The following is a narrative of transactions arising from the purchase of fixed assets during the year ended December 31:

Feb. 2. Invoice No. 48; purchased cabinet file for office use from The Gibson & Perin Co.; $120; terms, February 1 — 30 days. Estimated useful life, 10 years. Estimated trade-in value at end of 10 years, $30.

Mar. 6. Invoice No. 62; purchased a truck for delivery purposes from Dependable Motors, Inc.; $2,800; terms, March 4 — 30 days. Estimated useful life, 3 years. Estimated trade-in value at end of 3 years, $360.

April 8. Invoice No. 79; purchased an office desk from The H. & S. Pogue Co.; $72; terms, April 7 — 30 days. Estimated useful life, 20 years. No salvage value.

July 12. Invoice No. 104; purchased showcases from Economy Supply Co.; $360; terms, July 11 — 2/10, n/30. Estimated useful life, 15 years. No salvage value.

Aug. 18. Invoice No. 121; purchased double pedestal desk for use in storeroom from Royal Store Equipment Co.; $90; August 16 — terms 2/10, n/30. Estimated useful life, 20 years. No salvage value.

Sept. 19. Invoice No. 142; purchased Underwood typewriter, No. S5378852–11, from Underwood Typewriter Co.; $120; terms, September 18 — 30 days. Estimated useful life, 5 years. Estimated trade-in value at end of 5 years, $20.

REQUIRED: (a) Using an invoice record similar to the one reproduced on page 341 (except that a column will not be required for federal excise tax), record the foregoing transactions. (b) Foot the amount columns, prove the footings, enter the totals, and rule the invoice record. (c) Ascertain the annual rate of depreciation applicable to each of the fixed assets purchased, compute the amount of the depreciation sustained during the current year ended December 31, and draft an entry in general journal form to record the depreciation. (d) Assuming that on January 5, after recording twenty-two months' depreciation, the delivery truck purchased on March 6 was traded in for a new truck, $1,800 in cash being paid. Draft a general journal entry to record the transaction. (No gain or loss should be recognized.)

Problem 16-A

The Crew Builders Supply Co. is subject to the payroll taxes imposed under the Federal Insurance Contributions Act for old-age and survivors' insurance purposes. Employees on a weekly basis are paid on Saturday for the week just ended. Employees on a monthly basis are paid on the last day of the month for the month just ended. The following accounts are used in recording the social security taxes: Social Security Taxes and Social Security Taxes Payable. A list of the company's employees for the pay period ending Saturday, December 30, together with their wage rate, follows:

Joseph W. Harris	$ 40	per week	Mary Alice Keenan	$ 36	per week
Richard C. Nepper	250	per month	Catherine Feist	38	per week
Shirley Gels	38	per week	Frank K. Holliday	200	per month

REQUIRED: (a) Prepare in tabular form a report that will indicate for each employee (1) name, (2) wage rate, (3) amount of employees' tax withheld, (4) net amount paid each employee, and (5) amount of the employer's tax. Total the columns of the table. (b) Draft the required entries, in general journal form, to record the following: (1) The wages paid on December 30 and the amount withheld for federal old-age insurance purposes. (2) The amount of the tax imposed on the employer for federal old-age insurance purposes on a basis of the wages paid December 30. (3) A check for $99.78 issued to the collector of internal revenue on January 27 in payment of the federal old-age insurance taxes imposed for the quarter ended December 31.

Problem 16-B

The Richter Concrete Corporation is subject to social security taxes imposed under the federal laws for both old-age and survivors' insurance and for unemployment purposes. The following accounts are used in recording the social security taxes: Social Security Taxes, Federal Old-Age Insurance Taxes Payable, and Federal Unemployment Taxes Payable. During the month of June the corporation had in its employ the following individuals. The current wage rate of each individual is indicated.

T. F. Jewett	$ 36	per week	Victor F. Cooper	$280	per month
George Graver	40	per week	Lenora Steele	40	per week
Russell A. Cooper	42	per week	Edward A. Kleeman	44	per week
Thomas C. Snyder	220	per month	S. B. Berkeley	200	per month
Harry H. Ernst	240	per month			

REQUIRED: (a) Prepare in tabular form a report that will indicate for each employee (1) name, (2) wage rate, (3) amount of employee's tax withheld, (4) net amount paid each employee, (5) the amount of the employer's federal old-age insurance tax, and (6) the amount of the employer's federal unemployment tax. Total the columns of the table. (b) Draft a general journal entry to record the following: (1) The total wages for the pay period ending June 30. (2) The aggregate amount withheld from the employees' wages for federal old-age insurance purposes.

(3) The amount of the tax imposed on the employer for federal old-age insurance purposes. (4) The amount of the federal tax imposed on the employer for unemployment purposes. (5) The amount of the check issued to meet the June 30 payroll.

Problem 16-C

The Red Ball Transit Company, Inc. has eight employees. In addition to social security taxes imposed under the federal laws the company is required to make contributions to a state unemployment compensation fund amounting to 2.7% of the first $3,000 of wages earned by each employee. Employees on a monthly basis are paid for the half month just ended; employees on the weekly basis are paid for the week just ended. The following accounts are used in recording the social security taxes: Social Security Taxes, State Unemployment Contributions, Federal Old-Age Insurance Taxes Payable, Federal Unemployment Taxes Payable, and State Unemployment Contributions Payable. The payroll for the period ending December 31 follows:

L. H. Smart	$180 per month	Joseph Griffin	$ 38 per week
Mrs. Susie Murray	160 per month	L. E. Sheppard	320 per month
Irving Marcus	40 per week	Francis Leslie	240 per month
Julius Jager	38 per week	Lula Herron	36 per week

REQUIRED: (a) Prepare in tabular form a report that will indicate for each employee (1) name, (2) wage rate, (3) total earnings for the pay period, (4) F.I.C.A. taxable earnings for the pay period, (5) amount of employee's tax withheld, and (6) net amount paid each employee. Total the columns.

(b) Compute the taxes imposed on the employer on the basis of the total taxable wages for the pay period for (1) employer's federal old-age insurance tax, (2) employer's federal unemployment tax, and (3) state unemployment contributions.

(c) Draft the required entries, in general journal form, to record the following: (1) The December 31 payroll and payroll taxes. (2) The check for $133.08 issued to the collector of internal revenue on January 31 in payment of the federal old-age insurance taxes imposed for the quarter ended December 31. (3) The check for $53.59 issued to the collector of internal revenue on January 31 in payment of the federal unemployment taxes for the year ended December 31.

Problem 16-D

Kraus & Walsh pay their employees on the fifteenth and last day of each month, withholding the required amounts from their wages for federal income tax purposes. The November payroll transactions are as follows:

November 15. Payroll, $2,980; withheld for federal income tax purposes, $315.

November 30. Payroll, $3,120; withheld for federal income taxes, $330.

On December 9 a check was issued to First National Bank, a U. S. depositary, in payment of the federal income taxes withheld during November.

REQUIRED: Draft the general journal entries required to record the foregoing transactions.

Problem 16-E

L. M. Prince Co., opticians, are located in a state that imposes a consumers' sales tax of 3 per cent on the amount of each sale and requires the vendor to collect the tax from customers. A chronological record of charge sales is kept, the amount of the sale and the sales tax being recorded in separate columns. The total of cash sales for each day is entered in a record of cash receipts, the amount of the sales being recorded in one column and the sales tax in a separate column. The totals, by months, of the sales tax columns of the records of charge sales and cash sales kept by L. M. Prince Co. for the quarter ended March 31 follow:

	Consumers' Sales Tax Collected on Charge Sales	Consumers' Sales Tax Collected on Cash Sales
January	$ 92.16	$74.40
February	87.30	62.90
March	101.60	85.95

On April 12 the company filed a sales tax report and issued a check for the amount of the tax imposed on sales for the quarter ended March 31.

REQUIRED: (a) Open an account with Sales Tax Payable, Account No. 37, and post the monthly totals. (b) Draft the general journal entry required to record the payment of the tax, and post to the sales tax payable account. (c) Foot the account, and if the account is found to be in balance, enter the totals and rule the account.

Problem 18-A

Linger & Henderson are engaged as wholesale dealers in men's furnishings as partners. Their accounts are kept on the calendar year basis. The operating expense accounts are kept in a subsidiary ledger with a control account in a general ledger. Their accountant follows the practice of making any necessary adjustments in the operating expense accounts at the end of each month and provides the management with a monthly statement of operating expenses. The balances of the operating expense accounts on August 31, before making the monthly adjustments, were as follows:

711 Rent, $800
712 Salaries, $3,000
713 Advertising Expense, $452
714 Social Security Taxes, $21.50
715 State Unemployment Contributions, $27.90
716 Depreciation Expense, $248.75
717 Office Supplies Consumed, $320
718 Store Supplies Consumed, $365
719 Delivery Expense, $950
720 Loss on Bad Debts, $430
721 Insurance Expense, $212
722 Heat, Light, and Water, $428.30
723 Telephone and Telegraph, $180.60
724 Traveling Expense, $1,875
725 Miscellaneous General Expenses, $183.49

Following are the numbers and titles of the general ledger accounts that will be affected by the adjusting entries:

013 Reserve for Bad Debts
021 Reserve for Depreciation of Store Equip.
022 Reserve for Depreciation of Delivery Equip.
023 Reserve for Depreciation of Office Equip.
171 Store Supplies
172 Advertising Supplies
173 Office Supplies
174 Prepaid Insurance
37 Accrued Salaries Payable
71 Operating Expenses

The data for the adjusting entries at the end of August follow:

Depreciation of fixed assets during month:		
Store equipment	$ 7.50	
Delivery equipment	22.50	
Office equipment	14.80	$44.80
Store supplies consumed during month		62.30
Advertising supplies consumed during month		61.40
Office supplies consumed during month		32.95
Insurance expired during month		32.12
Increase in accrued salaries at end of month		54.60
Provision for bad debts		50.00

REQUIRED: (a) Using standard account forms, open accounts for the foregoing operating expense accounts and record the respective balances before the monthly adjustments are made. (b) Using columnar general journal paper, draft the entries required to adjust the operating expense accounts as of August 31. Foot the amount columns, prove the footings, enter the totals, and rule. (c) On the assumption that the posting from the general journal to the general ledger accounts affected has already been completed, insert the necessary check marks in the Folio column of the general journal; complete the posting from the general journal to the operating expense ledger accounts. (d) Foot the accounts in the operating expense ledger and prepare a schedule of the operating expenses as of August 31. Use two-column journal paper for the schedule.

Problem 18-B

Monce & Craig are partners engaged in the operation of a wholesale mercantile business. Their accounts are kept on the calendar year basis. Accounts with customers, creditors, and operating expenses are kept in subsidiary ledgers with control accounts in the general ledger. Any needed adjustments in the operating expense accounts are made at the end of each month before taking a trial balance. Since the accountant is required to prepare monthly financial statements, he follows the practice of preparing a ten-column work sheet at the end of each month as an aid to the preparation of a balance sheet and profit and loss statement.

REQUIRED: From the trial balance and adjustment data which follow, prepare a ten-column work sheet in complete form for Monce & Craig for the eleven-months' period ended November 30. (Allow 3 lines for Cost of Sales, Account No. 65.)

The following data provide the information needed in adjusting the general ledger accounts:

Merchandise inventory June 30, per stock records, $8,634.98
Interest accrued on notes receivable, June 30, $17.50
Interest accrued on notes payable, June 30, $11.50

MONCE & CRAIG

Trial Balance, November 30, 19--

Accounts	Nos.	Dr.	Cr.
Second National Bank	111	$ 8,899.33	
Petty Cash Fund	112	50.00	
Notes Receivable	131	2,200.00	
Accounts Receivable	132	4,170.61	
Reserve for Bad Debts	013		$ 120.00
Merchandise Inventory	15	9,334.15	
Accrued Interest Receivable	16	12.80	
Store Supplies	171	72.60	
Office Supplies	173	57.80	
Fuel	174	46.20	
Postage Stamps	175	72.60	
Prepaid Insurance	176	319.12	
Store Equipment	21	1,500.00	
Reserve for Depreciation of Store Equipment	021		123.45
Delivery Equipment	22	2,200.00	
Reserve for Depreciation of Delivery Equipment	022		520.00
Office Equipment	23	2,100.00	
Reserve for Depreciation of Office Equipment	023		295.00
Social Security Taxes Payable	31		51.90
Employees' Income Taxes Payable	32		105.40
Notes Payable	33		100.90
Accounts Payable	34		2,960.32
Accrued Interest Payable	35		14.00
E. H. Monce, Partner	41		8,212.80
E. H. Monce, Drawing	411	200.00	
A. E. Craig, Partner	42		8,212.80
A. E. Craig, Drawing	421	160.00	
Sales	511		61,290.80
Sales Returns and Allowances	0511	920.80	
Purchases Discount	521		612.00
Interest Income	522		28.40
Purchases	61	45,216.20	
Purchases Returns and Allowances	061		316.05
Transportation Inward	63	816.31	
Operating Expenses	71	4,249.50	
Sales Discount	751	346.40	
Interest Expense	752	19.40	
		$82,963.82	$82,963.82

Problem 19-A

Crosswhite & Cutshall are partners engaged in a merchandising enterprise. Their accounts are kept on the accrual basis and the books are closed at the end of the calendar year. Accounts with customers, creditors, and operating expenses are kept in subsidiary ledgers with control accounts in the general ledger. The operating expense accounts are adjusted at the end of each month. Monthly work sheets are used as an aid in preparing the financial statements. The necessary monthly adjustments in the general ledger accounts are made on the work sheet, but are not journalized and posted until the end of the year when the accounts are adjusted preliminary to closing the books.

The trial balance reproduced on the following page was taken on December 31 after making the necessary adjustments in the operating expense accounts for December. The following accounts which do not appear in the trial balance will be affected by the adjusting and closing entries at the end of the year:

65 Cost of Sales
43 Profit and Loss Summary

The data for adjusting the general ledger accounts at the end of the year follow:

Merchandise inventory, per stock records, $9,057.34
Interest accrued on notes receivable, December 31, $20.54
Prepaid interest expense, December 31, $9.65
Interest accrued on notes payable, December 31, $5.16

REQUIRED: As the accountant for Crosswhite & Cutshall, (a) prepare a ten-column work sheet for the year ended December 31 (when copying the trial balance on the work sheet, allow two lines for Interest Expense, Account No. 752, and three lines for Cost of Sales, Account No. 65); (b) prepare a balance sheet in account form as of December 31; (c) prepare a profit and loss statement for the year ended December 31; (d) using a columnar general journal, prepare the adjusting and closing entries required to close the books on December 31; (e) using standard account forms, open accounts for all of the accounts affected by the adjusting and closing entries, record the respective balances, post the adjusting and closing entries, and rule the accounts that are in balance; and (f) using two-column journal paper, take a post-closing trial balance to ascertain that the general ledger is in balance after closing the temporary accounts. (The balances of the general ledger accounts not affected by the adjusting and closing entries are the same as those stated in the trial balance.)

CROSSWHITE & CUTSHALL

Trial Balance, December 31, 19--

Accounts	Nos.	Dr.	Cr.
Cash in Bank	111	$ 5,416.12	
Petty Cash Fund	112	25.00	
Notes Receivable	131	2,842.30	
Accounts Receivable	132	5,997.83	
Reserve for Bad Debts	013		$ 352.85
Merchandise Inventory	15	12,742.02	
Accrued Interest Receivable	16	24.85	
Store Supplies	171	143.96	
Office Supplies	172	133.85	
Fuel	173	56.50	
Postage Stamps	174	169.25	
Prepaid Insurance	175	487.62	
Prepaid Interest	176	15.00	
Store Equipment	21	3,600.00	
Reserve for Depreciation of Store Equipment	021		648.18
Office Equipment	22	2,100.00	
Reserve for Depreciation of Office Equipment	022		193.40
Social Security Taxes Payable	31		88.56
Employees' Income Taxes Payable	32		162.12
Notes Payable	33		2,500.00
Accounts Payable	34		2,192.80
Accrued Interest Payable	35		4.35
Accrued Wages Payable	36		118.60
Accrued Property Taxes Payable	37		28.00
W. O. Crosswhite, Partner	41		9,867.39
W. O. Crosswhite, Drawing	411	612.50	
Paul Cutshall, Partner	42		9,820.39
Paul Cutshall, Drawing	421	593.85	
Sales	511		63,879.38
Sales Returns and Allowances	0511	341.80	
Purchases Discount	521		729.35
Interest Income	522		11.50
Purchases	61	39,316.49	
Purchases Returns and Allowances	061		297.20
Transportation In	63	909.43	
Operating Expenses	71	14,216.45	
Sales Discount	751	948.65	
Interest Expense	752	25.60	
Charitable Contributions	753	175.00	
		$90,894.07	$90,894.07

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